FILE COPY

Supreme Court, U. S.
FILED
SEP 21 1942
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1942.

Nos. 11-19

IN THE MATTER OF

CHICAGO, MILWAUKEE, ST. PAUL AND PACIFIC RAILROAD COMPANY,

Debtor.

GROUP OF INSTITUTIONAL INVESTORS AND MUTUAL SAVINGS BANK GROUP,

Petitioners,

vs.

CHICAGO, MILWAUKEE, ST. PAUL AND PACIFIC RAILROAD COMPANY, ET AL.,

Respondents.

BRIEF OF GROUP OF INSTITUTIONAL INVESTORS AND MUTUAL SAVINGS BANK GROUP, PETITIONERS.

KENNETH F. BURGESS,
DOUGLAS F. SMITH,
GEORGE RAGLAND, JR.,
Attorneys for Group of Institutional Investors.
FRED N. OLIVER,
WILLARD P. SCOTT,
Attorneys for Mutual Savings Bank Group.
SIDLEY, MCPHERSON, AUSTIN & BURGESS,
OLIVER & DONNALLY,
Of Counsel.

September 21, 1942.

THE GUNTHORP-WARREN PRINTING COMPANY, 210 WEST JACKSON, CHICAGO

INDEX.

	PAGE
Preliminary Statement	1
Opinions Below	2
Jurisdiction	3
Statement of the Case	3
(a) Proceedings Before the Commission	4
(b) Proceedings Before the Courts	5
(c) Debtor's Properties, Capitalization and Financial Structure	6
(d) Commission's Plan of Reorganization	11
(e) The Primary Issues Presented	14
Specifications of Error	21
Argument	22
I. The Decision Below Wholly Misconceives the Purpose of Congress in Enacting Section 77 and Renders That Statute Ineffective	22
(a) Authority Which Congress Intended Commission to Exercise Is Clearly Shown by the Statute, Its Legislative History and the Conditions of the Times Leading to Its Enactment	22
(b) The Commission's Plan as Approved by the District Court Effectuates the Congressional Intent, While the Decision of the Circuit Court of Appeals Would Nullify This New Legislation	29
II. The Plan Fully Complies With the Requirements of Section 77	33
(a) Requirements of the Statute	33
(b) Plans of Reorganization as Presented by the Parties and the Plan Approved by the Commission	34
(c) Changes in Plan Sought by Objectors Challenge the Determination of the Commission and the District Court on Matters Within Their Respective Jurisdictions	37

III. In Discharging Its Duties Under Section 77, the Commission Supported the Certified Plan by Reports Containing Comprehensive Findings and Conclusions 42

(a) The Commission Stated Its Findings in the Same Form That Has Repeatedly Been Determined by This Court to Be Adequate and Lawful 42

(b) Findings as to the Debtor's Property as a Whole 49

1. Determination of Amount and Character of New Securities Available for Distribution 49

2. Exclusion of the Old Preferred and Common Stocks 55

(c) Findings as to the Additions and Betterments Fund 64

(d) Findings as to Each of the Several Mortgage Divisions 68

1. General Mortgage 69

2. First and Refunding Mortgage 73

3. Fifty Year Five Per Cent. Mortgage 75

4. Convertible Adjustment Mortgage. 77

5. Milwaukee & Northern Mortgages. 79

6. The Terre Haute Lease 82

7. Chicago, Milwaukee & Gary Mortgage 94

(e) The Decision Below Is Not Required by the Opinion in the Consolidated Rock Products Case and Would Defeat the Purpose of Section 77 97

IV. Proceedings Should Be Remanded With Directions to Affirm Order of District Court Approving Commission's Plan of Reorganization 101

Appendix ..... i-vii

Table of Cases.

Akron, Canton & Youngstown Railway Company v. Hagenbuch, 128 F. (2d) 932 52

American Brake Shoe & Foundry Company v. New York Railways, 282 Fed. 523 89

Chicago, Milwaukee & St. Paul Reorganization, 131 I. C. C. 673 ..... 7, 22, 41, 61, 62, 63, 64

City and County of Denver v. Stenger, 295 Fed. 809 91

Colorado v. United States, 271 U. S. 153 ..... 42, 43

Consolidated Rock Products Co. v. DuBois, 312 U. S. 510 ..... 19, 30, 31, 66, 97, 100

Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island & Pacific Ry. Co., 294 U. S. 648 ..... 24, 28, 48, 102

Denver & Rio Grande Western Reorganization, 90 I. C. C. 141 40

Dickinson Co. v. Cowan, 309 U. S. 382 17

Federal Communications Commission v. Pottsville Broadcasting Co., 309 U. S. 134 32

Fifteen Percent Case, 226 I. C. C. 41 25

Florida v. United States, 292 U. S. 1 44

Gray v. Powell, 314 U. S. 402 32

Harris Trust & Savings Bank v. Chicago Rys. Co., 39 F. (2d) 958 91

Interstate Circuit, Inc. v. United States, 304 U. S. 55 45

Investigation of Chicago, Milwaukee & St. Paul Railway Company, 131 I. C. C. 615 ..... 22, 41, 62, 63, 83, 87, 94

Meeker and Co. v. Lehigh Valley R. R., 236 U. S. 412 44

New England Divisions Case, 261 U. S. 184 ..... 42, 43, 47

New York Central Securities Corporation v. United States, 54 F. (2d) 122; 287 U. S. 12 ..... 40, 56

1931 Fifteen Percent Case, Ex Parte 103, 178 I. C. C. 539 26
N., C. & St. L. Ry. v. Browning, 310 U. S. 362 ..... 48, 99
Oscar Heineman Corp. v. Nat Levy & Co., 6 F. (2d) 970 91
Palmer v. Massachusetts, 308 U. S. 79 ..... 27, 31, 66
Pennsylvania Steel Company v. New York City Railway Company, 198 Fed. 721 90
Pennsylvania Steel Company v. New York City Railway Company, 225 Fed. 734 90
R. R. Commission v. P. G. & E. Co., 302 U. S. 388 ..... 51, 52, 56
Reisenwebers v. Irving Trust Co., 293 U. S. 566 91
Revenues in Western District, Ex Parte 87, 113 I. C. C. 3 26
St. Louis Southwestern Ry. Co., In re, 252 I. C. C. 325 48
620 Church Street Building Corp., In re, 299 U. S. 24 .. 56
Story Parchment Co. v. Paterson Co., 282 U. S. 555 .. 104
Sunflower Oil Co. v. Wilson, 142 U. S. 313 91
United Cigar Stores of America, In re, 69 F. (2d) 513 91
United States v. Baltimore & O. R. Co., 293 U. S. 454 .. 44
United States v. Chicago, Milwaukee, St. Paul and Pacific Railroad Company, 282 U. S. 311 ..... 62, 63
United States v. Louisiana, 290 U. S. 70 ..... 43, 44, 45, 46
U. S. v. Morgan, 313 U. S. 409 99
Warren v. Palmer, 310 U. S. 132 39
Westinghouse Electric & Mfg. Co. v. Brooklyn Rapid Transit Co., 6 F. (2d) 547 91

STATUTES.

Bankruptcy Act, Sec. 77; 11 U. S. C. A. Sec. 205:
Subsection (b) 33, 38, 70, 83, 90, 91, 103
Subsection (c) 5, 34, 90

Subsection (d) 5, 17, 30, 33, 35, 42, 45, 48, 100
Subsection (e) 6, 17, 33, 39, 46, 57, 104

Interstate Commerce Act; 49 U. S. C. A.:
Sec. 14 45
Sec. 19a 47
Sec. 20a 22, 40, 41

Judicial Code, Sec. 240(a); 28 U. S. C. A. 347 3

Authorities.

Accounting Classifications Prescribed by the Interstate Commerce Commission 64
Finletter, The Law of Bankruptcy Reorganization 91
Fletcher, Cyclopedia of Corporations 91
Gresham, The Life of Walter Quintin Gresham 28
Interstate Commerce Commission 53rd Annual Report 62
Interstate Commerce Commission 54th Annual Report. 25
Jacobs, The Interstate Commerce Commission and Interstate Railroad Reorganizations, 45 Harv. L. Rev. 855 ..... 22, 42
Lowenthal, The Railroad Reorganization Act, 47 Harv. L. Rev. 18 22
72nd Congress, 2d Session, H. Rep. No. 1897 23
74th Congress, 1st Session, S. Rep. No. 1336, p. 46 ..... 27, 47
79 Cong. Record 13764 ..... 25, 27
79 Cong. Record 8851 25
Sharfman, The American Railroad Problem 61
Sharfman, The Interstate Commerce Commission 47
Statistics of Railways in the United States for Years 1930, 1935 and 1940 24
Taft, Recent Criticisms of the Federal Judiciary, Reports of the American Bar Association (1895) 23

IN THE

Supreme Court of the United States.

OCTOBER TERM, 1942.

Nos. 11-19.

IN THE MATTER OF

CHICAGO, MILWAUKEE, ST. PAUL AND PACIFIC RAILROAD COMPANY,

Debtor.

GROUP OF INSTITUTIONAL INVESTORS AND MUTUAL SAVINGS BANK GROUP,

Petitioners,

vs.

CHICAGO, MILWAUKEE, ST. PAUL AND PACIFIC RAILROAD COMPANY, ET AL.,

Respondents.

BRIEF OF GROUP OF INSTITUTIONAL INVESTORS AND MUTUAL SAVINGS BANK GROUP, PETITIONERS.

This cause is here on certiorari to review the judgments of the United States Circuit Court of Appeals for the Seventh Circuit, entered on December 4, 1940, in the reorganization proceedings for the Chicago, Milwaukee, St. Paul and Pacific Railroad Company reversing a judgment of the United States District Court for the Northern District of Illinois, Eastern Division, which had approved the plan of reorganization for that property under Section 77 of the Bankruptcy Act as certified to it by the Interstate Commerce Commission.

The petitioners on whose behalf this brief is filed are the Group of Institutional Investors, consisting of eleven life insurance companies[1], and the Mutual Savings Bank Group, consisting of approximately one hundred and fifty savings banks.[2] These fiduciary institutions own various securities of the debtor in the principal amount of approximately $84,000,000.

OPINIONS BELOW.

The reports and orders of the Interstate Commerce Commission are in 239 I. C. C. 485 and 240 I. C. C. 257. (Original Report, R. 2153-2269, and Order, R. 1258-1283; Supplemental Report, R. 1284-1317, and Order, R. 1319-1347) The opinion of the District Court is in 36 F. Supp. 193. (R. 1857-1899) The opinion of the Circuit Court of Appeals dated December 4, 1941, is in 124 F. (2d) 754. (R. 2297-2317). The *per curiam* opinion of the Circuit Court of Appeals dated January 12, 1942, on the petition to modify its opinion of December 4, 1941, is not reported. (R. 2334-5)

[1] The member companies of the life insurance group are the following:

Aetna Life Insurance Company.
John Hancock Mutual Life Insurance Company.
Metropolitan Life Insurance Company.
New England Mutual Life Insurance Company.
New York Life Insurance Company.
The Connecticut Mutual Life Insurance Company.
The Mutual Benefit Life Insurance Company.
The Northwestern Mutual Life Insurance Company.
The Penn Mutual Life Insurance Company.
The Prudential Insurance Company of America.
The Travelers Insurance Company.

[2] The savings banks which comprise this group are represented by a committee consisting of the following institutions:

Central Savings Bank.
Emigrant Industrial Savings Bank.
Institution for Savings in Roxbury.
Lynn Institution for Savings.
Philadelphia Savings Fund Society.
Savings Banks Trust Company.
Seamen's Bank for Savings.
Society for Savings.

JURISDICTION.

The judgments of the Circuit Court of Appeals were entered on December 4, 1941. (R. 2318-2324) The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by Act of February 13, 1925. (28 U. S. C. A., Sec. 347) The petitions for certiorari filed by these petitioners on January 17, 1942, and by the Solicitor General[1] on behalf of Reconstruction Finance Corporation (No. 38), were granted by this Court on June 8, 1942.[2]

STATEMENT OF THE CASE.

The Interstate Commerce Commission, in extended proceedings under Section 77 of the Bankruptcy Act (11 U. S. C. A., Sec. 205), has approved a plan of reorganization for the Chicago, Milwaukee, St. Paul and Pacific Railroad Company. This plan, after hearing, was approved by the United States District Court for the Northern District of Illinois, Eastern Division. Upon appeal, the Circuit Court of Appeals for the Seventh Circuit reversed the or-

[1] The Solicitor General also filed a memorandum on behalf of the Interstate Commerce Commission as *amicus curiae* urging that certiorari be granted.

[2] All of the appellants below, except two, filed petitions for certiorari, namely, interests representing the so-called Terre Haute bonds, No. 39; the debtor, No. 47; the General Mortgage trustee and certain General Mortgage bondholders, Nos. 51 and 55; the Fifty Year Five Per Cent. Mortgage trustees and Protective Committee, Nos. 52 and 53; and the Preferred Stockholders Committee, No. 54. The Court did not grant these petitions. The appellants below who did not ask certiorari are: (1) Union Trust Company, *et al.*, trustees and certain bondholders under the Gary mortgage (Circuit Court of Appeals No. 7610), and (2) certain Convertible Adjustment Mortgage bondholders (Circuit Court of Appeals No. 7611).

der of the District Court approving the plan and remanded the proceeding to the Interstate Commerce Commission.

The plan was certified by the Commission to the District Court on June 4, 1940, (R. 1319-1347) together with the Commission's report and order dated February 12, 1940, (R. 2153-2269), and its supplemental report dated June 4, 1940. (R. 1284-1317) On October 21, 1940, the District Court, after extended hearings, approved the plan in a comprehensive opinion, 36 F. Supp. 193 (R. 1857-1899), and on November 13, 1940, entered findings of fact, conclusions of law, and the order approving the plan. (R. 1978-1992) Upon appeal, the Circuit Court of Appeals by opinion and orders dated December 4, 1941, reversed the order of the District Court approving the plan and remanded the proceeding to the Commission. (R. 2297-2324) By opinion and order dated January 12, 1942, a motion of a committee of preferred stockholders for modification of the opinion of the Circuit Court of Appeals was denied. (R. 2334-2335)

(a) Proceedings Before the Commission.

Debtor's petition for reorganization under Section 77 of the Bankruptcy Act (11 U. S. C. A., Sec. 205), instituting the proceeding wherein the plan of reorganization was promulgated by the Interstate Commerce Commission, was filed with the United States District Court for the Northern District of Illinois, Eastern Division, and with the Interstate Commerce Commission on June 29, 1935 (R. 2-42), and by order on the same day the District Court approved the petition as properly filed. (R. 42-49). By order dated July 22, 1935, the Commission assigned the proceeding for hearing before it in Washington, D. C., on August 5, 1935. (R. 248)

Thereafter, public hearings were held by the Commission pursuant to Section 77(d) on August 5, 6 and 7, 1935, on June 16, 1937, on September 20, 1937, on February 1, 2, 3 and 4, 1938, and on March 21 and 22, 1938, which hearings were conducted by a member of the Commission, the Director of the Bureau of Finance, and an Examiner. The record before the Commission consists of the transcript of the oral testimony of witnesses at the hearings, numbering 1,666 pages, 219 statistical exhibits submitted by the parties, and a number of comprehensive studies prepared at the direction of the Commission pursuant to Section 77(c)(11), by its Bureaus of Valuation, Finance and Accounts.

The parties filed several sets of briefs before the Commission. On November 5, 1938, the Commission's Examiner issued a proposed report on a plan of reorganization. (R. 1162-1239) Oral arguments were heard by the entire Commission on April 12, 1939. The initial report and order of the Commission approving a plan of reorganization were issued on February 12, 1940. (R. 1258-1283; 2153-2269) Petitions for modification of the plan were filed on behalf of the numerous parties, and answers were filed to those petitions. On June 4, 1940, the Commission issued a supplemental report and order by which it modified the plan in certain respects, and, as modified, approved and certified the plan to the District Court. (R. 1284-1317; 1319-1347)

(b) Proceedings Before the Courts.

The District Court held hearings on objections to the plan and on claims for equitable treatment in respect thereto on September 4, 5, 6, 9, 10, 11, 12 and 13, 1940. Voluminous oral and documentary evidence was introduced before the court in addition to the record made be-

fore the Commission, and the matter was extensively argued by counsel. On October 21, 1940, the District Court approved the plan in a comprehensive opinion (R. 1857-1899), and its order of approval was entered on November 13, 1940. (R. 1978-1992)

On February 18, 1941, the Circuit Court of Appeals, upon the *ex parte* motion of the debtor, stayed submission of the plan by the Commission to the creditors for acceptance or rejection pending the appeals, notwithstanding the fact that the Commission was proceeding under the explicit direction of Section 77(e) that upon approval by the judge "the plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed • • • for acceptance or rejection." (R. 2274) On April 7, 1941, and again on June 18, 1941, the Circuit Court of Appeals denied motions and petitions filed by the Interstate Commerce Commission, the Reconstruction Finance Corporation and these petitioners to dissolve the stay of submission. (R. 2287, 2296)

On December 4, 1941, after consideration of the appeals on briefs and arguments of the parties, the Circuit Court of Appeals reversed the order of the District Court approving the plan and remanded the proceeding to the Commission. (R. 2297-2324) On January 12, 1942, it denied a motion of the committee representing preferred stockholders to modify its opinion. (R. 2334-5)

(c) Debtor's Properties, Capitalization and Financial Structure.

Debtor's railroad system consists of approximately 11,115 miles of railroad operated in twelve states, of which 9,906 miles are wholly owned. (R. 2162) Its lines extend from Chicago, Milwaukee, and other eastern termini to Seattle and Tacoma on the Pacific Coast, with intermediate termini at Kansas City, Minneapolis, St. Paul and Omaha. At

the time the record was made up its equipment comprised 1,260 locomotives, 56,309 revenue freight cars, 3,772 units of non-revenue freight equipment, and 980 passenger train cars. (R. 2162)

This property has been in receivership or bankruptcy for approximately eleven of the last eighteen years. Debtor came into existence in 1928 as a reorganized railroad following an equity receivership which began in 1925. The effect of that reorganization, while reducing the fixed charges from $21,544,066 to $13,663,489 (R. 2166), was actually to increase the total capitalization from $698,974,875 to $707,651,549, and the total charges, fixed and contingent, from $21,544,066 to $22,807,174, and in addition to provide contingent sinking fund charges of $1,139,368 per annum beginning in 1936. (Chicago, Milwaukee & St. Paul Reorganization, 131 I. C. C. 673, table at p. 723; R. 2165-2166) In the years following its reorganization the debtor earned its fixed charges only in 1928, 1929 and 1930. (R. 2180) In 1932 it reported an operating deficit. (R. 2180)

The annual interest charges on debt in 1935, when the petition for reorganization was filed, were approximately $14,458,250 fixed interest and $9,143,685 contingent interest, or a total of $23,601,935. (R. 24) On January 1, 1939, which the Commission found should be the effective date of its plan of reorganization, the debt, including accrued and unpaid interest, amounted to $626,926,331 (R. 1317), on which, at the average rate of interest on its outstanding bonds of 4.7 per cent (R. 790), the annual interest required to service such debt was $29,465,537. This amount may be compared with the annual earnings of the property during the eighteen-year period from 1921 to 1938, inclusive, which were before the Commission when it promulgated its plan of reorganization, and were, as shown in its report (R. 2180) as follows:

INCOME AVAILABLE FOR PAYMENT OF INTEREST.

	As Reported by Carrier	As Modified by Committee[1]
1921	$ 7,985,488	$ 8,801,859
1922	13,222,720	14,506,448
1923	20,379,860	23,339,726
1924	18,992,891	20,39[illegible],452
1925	16,846,185	19,126,107
1926	18,369,990	21,128,190
1927	14,189,866	17,805,810
1928	30,671,632	32,885,369
1929	29,105,102	31,354,184
1930	17,938,346	20,298,074
1931	9,202,933	11,384,238
1932	*232,590* (Def.)	2,680,530
1933	8,628,145	11,185,699
1934	6,719,954	8,831,558
1935	4,905,940	5,213,501
1936	9,706,089	12,298,916
1937	8,687,380	8,224,809
1938	4,962,923	6,023,296
18 Year Average	$13,349,047	$15,304,822

Debtor's financial structure presented the usual complications common to large railroad systems. There are four large mortgages, the General Mortgage, the First and Refunding Mortgage, the Fifty Year Five Per Cent. Mortgage, and the Convertible Adjustment Mortgage. These, because of the nature of their respective liens, have many characteristics of divisional mortgages and present the reorganization difficulties inherent therein. Thus the General Mortgage, with $138,788,000 principal

[1] The Commission said: "The amounts stated by the committee represent the adding back of the Terre Haute rental, and with respect to the years 1931 to 1935, inclusive, certain modifications of the charges to depreciation and retirement of equipment, amortization of debt discount, taxes due to the State of Washington, and charges under the Railroad Retirement Act not actually incurred. It is stated in the debtor's brief that neither the accuracy nor the propriety of these adjustments is questioned." (R. 2180)

amount of bonds outstanding in the hands of the public and $11,212,000 principal amount held by the Reconstruction Finance Corporation as collateral security for loans, is a first lien generally on debtor's lines east of the Missouri River. The First and Refunding Mortgage, of which all the outstanding bonds in the principal amount of $8,923,000 are held by the Reconstruction Finance Corporation as collateral security for loans, is a first lien generally on the lines west of the Missouri River and a second lien on the lines east of the Missouri River. The Fifty Year Five Per Cent. Mortgage, with $106,395,096 principal amount of bonds outstanding, is, subject only to this Reconstruction Finance Corporation claim, the prior lien on the lines west of the Missouri River and the lien next in order after the General Mortgage on the lines east. The Convertible Adjustment Mortgage, with $182,873,693 principal amount of bonds outstanding, is the most junior lien on the lines west and on the lines east. (R. 2166, 2170-2171, 2172) Of these several mortgages the General Mortgage survived the receivership of 1925-1928 (R. 2165), while the other mortgages were placed on the property as a part of that reorganization.

In addition to these four mortgages debtor had assumed liability on the bonds of certain small companies whose properties it or its predecessor had acquired by purchase or lease. These consist of two issues of bonds of the Milwaukee & Northern Railroad Company, being the Milwaukee & Northern first mortgage bonds, $2,117,000 principal amount outstanding, secured by a first lien on 110 miles of line south of Green Bay, Wisconsin (R. 2167-2168), and Milwaukee & Northern consolidated mortgage bonds, $5,072,000 principal amount outstanding, secured by a first lien on 286 miles of line north of Green Bay and a second lien on the line south of that point (R. 2168); an issue of Chicago, Milwaukee & Gary first mortgage bonds, $3,000,000 principal amount outstanding, secured by a first lien on

83 miles of disconnected portions of track originally projected as an outer belt line around the Chicago district (R. 1308-1309, 2170); and four issues of bonds of the Chicago, Terre Haute and Southeastern Railway Company and its subsidiaries, aggregating $21,929,000 principal amount outstanding, secured by respective liens on various parts of 298 miles of main line and certain branch line and trackage rights in western Indiana, which are operated by the debtor under a 999 year lease. (R. 2163, 2169) In addition, the debtor had pledged to the Reconstruction Finance Corporation $301,000 principal amount of first mortgage bonds of the Bellingham Bay & British Columbia Railroad Company secured by a first lien on 67 miles of line in the State of Washington. (R. 2172)

The properties subject to the Milwaukee & Northern mortgages, the Chicago, Milwaukee & Gary mortgage, and the Bellingham Bay & British Columbia mortgage, and also the debtor's leasehold interest in the Chicago, Terre Haute and Southeastern and its subsidiaries, are thereafter subject to the respective liens, in the order named, of the First and Refunding Mortgage, the Fifty Year Five Per Cent. Mortgage, and the Convertible Adjustment Mortgage. (R. 2171, 2172) Not only are large amounts of accrued interest unpaid (on December 31, 1938, this amounted to $118,878,918, R. 1317), but under the several mortgages numerous defaults exist through failure to replace and maintain equipment pledged thereunder and in other respects.

Debtor is also indebted to the Reconstruction Finance Corporation in the principal amount of $12,920,463, heavily secured by the pledge of collateral, and on the Trustees' note to the Continental Illinois National Bank and Trust Company in the principal amount of $1,184,000.[1] (R. 2173, 2174)

[1] This note was for money borrowed to pay taxes and has since been paid.

Debtor's obligations on notes issued under various equipment trusts and secured by equipment purchased with moneys thereby received were outstanding on December 31, 1938, in the principal amount of $33,322,999, and unsecured claims against it as of September 30, 1937, amounted to $445,162. (R. 1317)

(d) Commission's Plan of Reorganization.

The capitalization of the new company as determined by the Commission and approved by the District Court is based upon an exhaustive study of all of the elements of value usually considered by courts and commissions, including the earning power of the property, past, present and prospective, cost of reproduction new and less depreciation, the original cost of the property, and the actual investment therein, all weighed in the light of the public interest as the statute requires. As a substitute for its exceedingly complex corporate structure under which the debtor had long been unable to meet its fixed and contingent interest charges, the Commission's plan provides two system mortgages. One is the new first mortgage to be secured by a first lien on all properties owned by the debtor, subject only to the lien of equipment obligations, and under it the Commission provided for the issuance at reorganization of $58,923,171 of new 4% fixed interest bonds. The other is the new general mortgage which is to constitute a lien, subject to the lien of the first mortgage, on all property from time to time under the lien of that mortgage. Provision is made for the issuance under the new general mortgage at reorganization of two series of bonds carrying interest contingent upon earnings at the rate of 4½%, series A bonds in the principal amount of $57,256,669 and series B bonds in the principal amount of $51,422,111. (R. 1317, 2226-2235)

The Commission's plan provides for the issuance of 5% preferred stock of the reorganized company in the amount

of $111,347,846, together with 2,131,475¼ shares of no-par common stock. (R. 1317, 1336, 1338) The plan requires that an additions and betterments fund be set up annually in the amount of $2,500,000, as a charge ahead of contingent interest, for purposes specified in detail in the plan, and provides that the board of directors may set aside certain additional amounts for the same purposes after payment of full interest on the new general mortgage series A bonds and the modified Terre Haute bonds. (R. 1332-1335)

Under the Commission's plan, the annual fixed charges of the reorganized company at reorganization would aggregate $4,269,654 and its contingent interest charges, $5,219,480, the latter following the charge for the mandatory fund for additions and betterments of $2,500,000, and followed by a sinking fund for reduction of debt, of approximately $543,394 annually. (R. 1317)

To summarize, the Commission found the permissible capitalization to be $548,533,321, made up as follows:

Fixed interest debt securities in the amount of	$108,780,470
Contingent interest debt securities in the amount of	115,257,480
5% preferred stock	111,347,846
Common stock (no par but taken at $100 per share)	213,147,525
Total new capitalization	$548,533,321

The permissible capitalization thus fell far short of the existing debt of $626,926,331, at the effective date of the plan (R. 1317), and the Commission found that the equity of the debtor's preferred and common stockholders had no value, and that such stockholders were not entitled to participate in the plan. (R. 2260)

In the allocation of securities to creditors of the debtor, the Commission first deducted from the permissible fixed interest debt of $108,780,470, the amount of equipment obli-

gations and the Trustees' note to the Continental Illinois National Bank and Trust Company, together aggregating $34,506,999, which were so well secured as to remain undisturbed in the reorganization. (R. 1317, 2218, 2246) Next, because it found that "the margin of security for these loans [the Reconstruction Finance Corporation loans] is unusually large" (R. 2247), the Commission allocated new first mortgage bonds to the Reconstruction Finance Corporation for 100% of its claim in the amount of $11,947,164, after reducing the amount of the claim by certain cash credits. (R. 1317, 2246-2248) That left a balance of $62,326,307 of new fixed interest securities together with the contingent interest securities and the preferred and common stock provided by the new capitalization for distribution among all remaining creditors. In making this allocation the Commission dealt first with the debtor's secured creditors and then with its unsecured creditors, the latter class consisting of holders of the Adjustment Mortgage bonds in respect of their deficiency claims and general claimants. The Commission determined the respective lien positions of the several mortgages, the relative earning value of each line, the elements of physical value thereof, and other relevant factors, as is set forth *infra* on pages 68 to 97 of this brief. The new bonds and stocks allotted in discharge of the debts existing under the debtor's seven mortgages described above, are in the relative amounts and proportions which the Commission in its plan found to be fair and equitable. (R. 1317)

The Commission's plan also provided that an offer be made to the bondholders of the Chicago, Terre Haute and Southeastern Railway Company and its subsidiaries for their voluntary acceptance or rejection. The offer provides that the reorganized company will lease the Terre Haute line only if the interest rates on the Terre Haute bonds are modified so that they will bear fixed interest at

2.75% per annum and, in addition, interest at 1.5% contingent on system earnings on the same basis as the new general mortgage bonds, series A, the maturities of the four existing mortgages are extended, and equipment vacancies are waived. If the offer is not accepted, the lease is to be rejected as of the date of the determination by the District Court that the offer has not been accepted by substantially all of the Terre Haute bondholders. (R. 2216-2218)

The holders of preferred and common stock of the debtor which was found by the Commission to be of no value, as previously noted, were given no participation in the reorganized company. (R. 1341) Likewise the plan required cancellation of more than $83,000,000 of claims of creditors.

The Commission's plan of reorganization thus provided the permissible capitalization of the reorganized company and the fair and equitable manner in which this capitalization should be distributed among the creditors of the debtor in order to discharge their claims and so permit the reorganized company, conformable to the public interest, to furnish essential transportation service.

For convenience, the present capitalization of the debtor, the new capitalization and distribution under the plan of reorganization, certified by the Commission and approved by the District Court, are reprinted on the opposite page as shown in the table attached to the Commission's supplemental report. (R. 1317)

(c) The Primary Issues Presented.

In the plan of reorganization, duly certified to the District Court, the Commission, in specific and categorical terms, defined the treatment which it found to be fair and equitable for every interest, and in accompanying reports, consisting of 144 pages, the Commission stated the basis for its conclusions in fact and in law in compliance with the

CHICAGO, MILWAUKEE, ST. PAUL AND PACIFIC RAILROAD COMPANY REORGANIZATION

(Appendix to Commission's Supplemental Report, R. 1317)

Present Obligations and Stock				Approved Plan as modified						
	Principal Amount	Interest accrued to Dec. 31, 1938 and not authorized to be paid	Total	Undisturbed or Extended	First Mortgage Bonds	General Mortgage 4½% Bonds Series A	General Mortgage 4½% Bonds Series B convertible	5% Preferred Stock	Common Stock No-par Value shares	
					(4% interest except Terre Haute bonds)					
Equipment obligations	$ 33,322,999	$	$ 33,322,999	$ 33,322,999		$	$	$		
					(100%)					
R. F. C. loans	12,920,463		12,920,463 (a)		$ 11,947,164					
Note to Cont. Ill. Nat. B'k & Trust Company	1,184,000		1,184,000	1,184,000						
Terre Haute bonds:										
So. Ind. Ry. 4s, 1951	7,287,000		7,287,000		7,287,000)					
Bedford Belt Ry. 5s, 1938	250,000		250,000		250,000)					
T. H. first & ref. 5s, 1960	8,056,000		8,056,000		8,056,000)	See Note.				
T. H. income 5s, 1960	6,336,000		6,336,000		6,336,000)					
					(70%)	(30%)				
Mil. & Nor. R. R. bonds:										
First mtg. 4½s, 1939	2,117,000	103,204	2,220,204		1,554,143	666,061				
					(25%)	(35%)	(20%)	(20%)		
Consol. mtg. 4½s, 1939	5,072,000	247,260	5,319,260		1,329,815	1,861,741	1,063,852	1,063,852		
General Mtg. bonds, 1989:					(25%)	(35%)	(20%)	(20%)		
Series A, 4s	48,241,000	5,653,090	53,894,090		13,473,523	18,862,931	10,778,818	10,778,818		
Series B, 3½s	8,950,000	920,211	9,870,211		2,467,553	3,454,574	1,974,042	1,974,042		
Series C, 4½s	42,597,000	5,652,191	48,249,191		12,062,298	16,887,217	9,649,838	9,649,838		
Series D, 4½s	24,000,000	3,217,320	27,217,320		6,804,330	9,526,062	5,443,464	5,443,464		
Series E, 4¾s	15,000,000	2,137,381	17,137,381		4,284,345	5,998,083	3,427,476	3,427,476		
							(15%)	(60%)	(25%)	
50-yr. mtg. 5s, 1975	106,395,096	20,835,706	127,230,802				19,084,621	76,338,481	318,077	
Convert.—Adjust. mtg. 5s, 2000	182,873,693	79,550,055	262,423,748						1,749,492	
									39,163 (c)	
								(75%)	(25%)	
Gary first mtg. 5s, 1948	3,000,000	562,500	3,562,500					2,671,875	8,906¼	
					5,000,000	(Assumed amount of new money bonds issued in reorganization. Interest assumed at 4%.)				
Unsecured claims (9/30/37)	445,162		445,162							
Total debt	508,047,413	118,878,918	626,926,331						15,837 (d)	
Preferred stock	119,307,300			No equity						
Common stock, no-par value	1,174,060 shs. (b)			No equity						
Totals, New Company				34,506,999	58,923,171	57,256,669	51,422,111	111,347,846	2,131,475¼	
Terre Haute					21,929,000	(See Note)				

SUMMARY	Principal Amount	Annual Charges
Equipment obligations, to be assumed; maturities to be rearranged in part	$ 33,322,999	$ 1,286,000
Bank note, undisturbed	1,184,000	23,680
First Mtg. bonds of new company	58,923,171	2,356,927
New Terre Haute bonds; portion representing fixed interest	15,350,300	603,047
Total fixed int. debt	108,780,470	4,269,654
Adds.—Betts. fund; mandatory payment		2,500,000
Gen. mtg. 4½% income bonds of new company	108,678,780	4,890,545
New Terre Haute bonds, portion representing contingent interest	6,578,700	328,935
Total system debt	224,037,950	
Sinking fund, approx		543,394
Charges ahead of dividends		12,532,528
New 5% preferred stock	111,347,846	5,567,392
New no-par common stock, shown at $100 a share	213,147,525	
	548,533,312	

Percent of debt to total capitalization.—40.8

Note: These items, strictly not a part of the capital structure of the new company, are included here since, under the plan, the new company will assume obligation with respect to principal and interest of the four classes of Terre Haute bonds, if the terms thereof are modified as provided in the plan. Such modification included the provision that the bonds will bear fixed interest at the rate of 2.75 percent and contingent interest at the rate of 1.5 percent per annum.

(a) Reflecting repayment of $290,000 Jan. 3, 1939. Further reduced for purpose of the plan by crediting $973,299 cash in hands of first and refunding mtg. trustee Dec. 29, 1938, leaving $11,947,164 to be discharged by issue of new securities.

(b) Not including capital stock of the Terre Haute. Of such stock 1,259 shares are not owned by the Milwaukee.

(c) Additional common stock assigned on basis of free assets.

(d) Other additional common stock issued on the basis of free assets; to be issued to holders of unsecured claims as provided in the plan.

requirement of Section 77, that "the Commission shall state fully the reasons for its conclusions." (Sec. 77(d))

The District Court, in the exercise of an independent judgment on the record before it, held that the plan was supported by the evidence, that it was in all respects a lawful plan, and on that basis approved it. Subsection (e) of Section 77 which states the prerequisites to approval of the plan by the judge provides:

> "After such hearing, and without any hearing if no objections are filed, *the judge*[1] *shall approve the plan if satisfied that*: (1) It complies with the provisions of sub-section (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) * * *"

The District Court conducted an extensive hearing on the objections to the plan and in its opinion, after quoting the foregoing provision of the statute, stated:

> "It is apparent that it was intended by the law that the Bankruptcy Court and the Interstate Commerce Commission should cooperate to the end that a fair and equitable Plan of Reorganization might be provided. Such purpose has been declared in a recent decision of the Supreme Court of the United States in *Warren* v. *Palmer*, 84 L. Ed. 752; 310 U. S. 132.
>
> "That Court has not yet determined just what weight should be given by the Court to the findings and conclusions of the Commission. Clearly, the Court has power to correct errors of law into which the Commission may have fallen and to set aside findings of fact which are not supported by the record or conclusions which violate constitutional rights. On

[1] The word "judge" means "a judge of a court of bankruptcy," "the district court," and "such court does not include the circuit court of appeals." (*Dickinson Co.* v. *Cowan*, 309 U. S. 382, 383-384 (1940).) All italics in this brief have been added.

> the other hand, the initial determination of the questions bearing upon the soundness and reasonableness of a Plan of Reorganization is the responsibility of the Commission which is peculiarly fitted for the consideration of such questions and its findings and conclusions, made and reached after extended hearings and exhaustive study, as in this case, should be given great weight." (R. 1870)

Expressing the view that this Court had not determined the effect to be given the findings of the Commission, the District Court, while according great weight to the Commission's findings, very properly reached its own conclusion in respect to every essential feature of the plan and, being thus "satisfied" that the plan complies with the requirements of Section 77, approved it. The Circuit Court of Appeals held that the District Court erred in thus sustaining the Commission's plan notwithstanding the fact that the District Court did so in the exercise of an independent judgment on the record before it, and that the Circuit Court of Appeals itself found that "there is evidence in the record to support the plan as proposed." (R. 2314) This holding by the Circuit Court of Appeals raises the primary question in the case.

The Circuit Court of Appeals sustained the Commission's finding that the stock is without value, and held that any different finding would not have been supported by evidence. (R. 2309-11) On motion to modify opinion the court further held, on January 12, 1942:

> "Now, to make our position entirely clear, we add this memorandum and hold that the finding of the I. C. C. as to absence of value of old common and preferred stock, is specific, definite and certain, and fully meets the rule which requires finding on values of assets.
>
> "Second, we meant to hold, and do hold, that the evidence supports this finding, that there is no value to either the common or preferred stock of debtor." (R. 2335)

As to other objections to the plan, the Circuit Court of Appeals held that "The plan as such, ignoring the absence of findings, has support in the evidence. It violates no requirements (save findings) announced in the *Consolidated Rock Products case.*"[1] (R. 2312) The court also stated:

> "• • • It may be observed that in our opinion there is evidence in the record to support the plan as proposed, but it cannot receive final approval until and unless there are findings made upon such evidence, and then the parties interested may have the right to review both the sufficiency of the findings to support the plan and the existence of evidence to support the findings." (R. 2314)

In view of its conclusion that the evidence supported the plan, the Circuit Court of Appeals expressed reluctance that it must reverse the District Court's order approving the plan, but deemed it necessary to do so under its interpretation of the *Consolidated Rock Products* case. The court seemed to interpret that case as setting up a technical requirement that a formal finding of fact be made on each step in the process of reasoning which impelled the Commission to its conclusions, notwithstanding the court's own holding that "there is evidence in the record to support the plan as proposed." (R. 2314) The court said:

> "We appreciate that the findings of fact must, in the last analysis, be based upon evidence, much of which is to be found in the report of the I. C. C. • • • Reluctant as we are to do so, we nevertheless feel that under the decision of this controlling case, there must be a return of the cause to the District Court with direction to the District Court to return it to the I. C. C. and for that body to make the findings on issues vital to the question of values and equities as announced in said *Consolidated Rock Products case.*" (R. 2315)

What we believe to be the extreme nature of the court's holding may be illustrated by its view respecting various

[1] *Consolidated Rock Products Company* v. *Du Bois*, 312 U. S. 510 (1941).

features of the plan specifically found by the court to be warranted by the record, yet disapproved as lacking adequate supporting findings. For example, the court decided that the provision in the plan for an additions and betterments fund for the reorganized company, found to be necessary by the Commission to assure performance of the road's public function, must be disapproved for lack of findings to "support both the allowance and the amount of the allowance." (R. 2313) This conclusion was reached despite the fact that the District Court was satisfied that the provision was sound and the fact that the Circuit Court of Appeals itself found that the evidence "would amply warrant an allowance for such an item, and also the amount adopted by the Commission." (R. 2313)

The Circuit Court of Appeals, denying any effect to the statutory approval of the District Court, held the plan certified by the Commission to be deficient not in substance, but in form. It is unnecessary to go beyond the opinion of the Circuit Court of Appeals itself to show that the plan and accompanying report were in such form as to enable the court, on the record before it, to review the decision of the District Court upholding the plan. Having found that "there is evidence in the record to support the plan as proposed," it is obvious not only that the court was in a position to perform its function under the statute, but that in so finding, it did, in effect, and within the contemplation of the statute, sustain the judgment of the District Court that the plan is fair, equitable and lawful.

SPECIFICATIONS OF ERROR.

The Circuit Court of Appeals erred:

1. In holding that a plan of railroad reorganization, which is held by it to be supported by the evidence, and approved by the District Court on that ground, which values the claim of every creditor in terms of new securities and is accompanied by reports fully setting forth the Commission's reasons for its conclusions, should be disapproved for lack of more specific determinations of value.

2. In holding that when the Commission has determined that an additions and betterments fund must be established to enable the property to perform its public function, and upon a full review and consideration of the experienced and anticipated needs of the carrier has prescribed the amount of such fund, *and the Circuit Court of* Appeals has found that "there is evidence that would amply warrant an allowance for such an item, and also the amount adopted by the Commission" (R. 2313), there must be further findings "which support both the allowance and the amount of the allowance." (R. 2313)

3. In holding that where the Commission has certified a plan of reorganization to the District Court as fair and equitable, together with reports finding the amounts and character of the various claims, the security therefor, the earning power and physical value of the property as a whole and by mortgage divisions, and the Circuit Court of Appeals sustains the holding of the District Court that the evidence in the record supports the plan, the plan must nevertheless be disapproved and the reorganization proceeding be remanded to the Commission for the purpose of fixing "values" of each mortgage division or for other more specific findings.

4. In failing to affirm the District Court's order approving the Commission's plan of reorganization.

ARGUMENT.

I.

THE DECISION BELOW WHOLLY MISCONCEIVES THE PURPOSE OF CONGRESS IN ENACTING SECTION 77 AND RENDERS THAT STATUTE INEFFECTIVE.

(a) Authority Which Congress Intended Commission to Exercise Is Clearly Shown by the Statute, Its Legislativ History and the Conditions of the Times Leading to Its Enactment.

By enacting Section 77 of the Bankruptcy Act in 1933, Congress for the first time made railroads subject to bankruptcy legislation. (11 U. S. C. A. 205, Public No. 420, 72nd Congress, approved March 3, 1933, 47 U. S. Stat. 1474) Prior to that legislation, railroads had been reorganized through the medium of equity receiverships and the Commission had power, under Section 20a of the Interstate Commerce Act, only to grant or to refuse authorization for issuance of the new securities necessary to carry out a plan of reorganization already approved by the courts. In the administration of that section of the act the Commission was confronted with the dilemma of either authorizing the issuance of the proposed securities or of vetoing the plan of reorganization after it had been evolved in its completed form through the long and burdensome processes of an equity receivership. The Commission found this situation fundamentally undesirable and had so stated in its investigation of the 1928 reorganization proceedings of debtor's predecessor, the Chicago, Milwaukee and St. Paul Railway Company.[1]

---

[1] Investigation of Chicago, Milwaukee & St. Paul Railway Company, 131 I. C. C. 615, 671 (1928); Chicago, Milwaukee & St. Paul Reorganization, 131 I. C. C. 673, 694, 699 (1928); Lowenthal, The Railroad Reorganization Act, 47 Harv. L. Rev. 18; Jacobs, The Interstate Commerce Commission and Interstate Railroad Reorganizations, 45 Harv. L. Rev. 855, 878, footnote 111.

Reorganization of railroads through the processes of equity receivership had also been criticized as expensive, failing to protect unorganized holders of securities, and ignoring or subordinating the public interest in the evolution of a plan of reorganization by means of barter and trade between conflicting creditor and stockholder interests.[1] It was the 19[illegible] reorganization of the debtor's predecessor and the widespread public criticism which it evoked, that was largely responsible for the enactment of the new legislation in 1933, entrusting to the administrative processes of the Commission the primary responsibility and duty of promulgating the plan of reorganization.

The history of Section 77, as it was enacted in 1933, discloses that the evil or mischief sought to be remedied had to do with a lack of uniformity of treatment in prior reorganizations in respect to railroad capitalization, distribution of securities among creditors, allowance of fees and, above all, the large public interest in transportation systems vital to the welfare of the nation. Demand for the immediate enactment of remedial legislation was precipitated by the fact that the decline in railroad earnings following the depression which began with the stock market crash in October, 1929, signalized the approach of another era of railroad defaults and reorganizations which threatened to outrun the catastrophes of

[1] The Committee on Judiciary of House of Representatives on January 23, 1933, in reporting favorably on H. R. 14359, which, with certain amendments, was enacted as Section 77 of the Bankruptcy Act, stated: "The necessity for the enactment of this section grows out of the present expensive, protracted, confusing, and inefficient administration of affairs of railroad companies engaged in interstate commerce in equity receiverships." (H. Rep. No. 1897, 72d Congress, 2d Session, p. 5). See also recommendation of President Taft in his message to Congress in 1910, 45 Cong. Rec. 463, and his earlier suggestion for administrative action in 1895 when Circuit Judge in an address before the American Bar Association. Taft, Recent Criticisms of the Federal Judiciary, Reports of the American Bar Association (1895), pp. 237, 264.

1893, 1907 and 1913-1915, periods marked by many railroad failures.[1]

The urgency was such that the 1933 amendment to the Bankruptcy Act which placed Section 77 in the statutes was hastily enacted. Two years later Congress undertook a further and more deliberate consideration of the principles involved in this legislation. In the meantime the economic condition of the railroads had greatly worsened. A large number of railroads had filed petitions to reorganize under the law, and it was apparent that many more would soon be compelled to do likewise. While the constitutionality of the Section had been sustained by this Court (*Continental Illinois National Bank & Trust Co.* v. *Chicago, Rock Island & Pacific Ry. Co.*, 294 U. S. 648), it was realized that some amplification of the authority and duty of the Interstate Commerce Commission was required to effectuate the railroad reorganizations which Congress then knew were inevitable. Intensive study was made and a revised Section drafted by the Federal Coordinator of Transportation, Hon. Joseph B. Eastman.[2]

The background of this legislation is most important in determining the jurisdiction with which Congress invested the Commission in preparing to meet the avalanche of railroad bankruptcies which was known to be imminent.

---

[1] High points of railroad mileage in the hands of receivers and trustees have been: June 30, 1894, 40,819 miles; June 30, 1915, 37,353 miles; December 31, 1935, 68,345 miles; and December 31, 1940, 75,270 miles. *I. C. C. Statistics of Railways in the United States* for years 1930 and 1935, Statement No. 5 and for year 1940, Table No. 151.

[2] H. R. 6249, drafted by counsel for the Coordinator of Transportation, was reported by the House Committee on the Judiciary, with minor revisions, as H. R. 8587. (74th Congress, First Session, H. Com. Rep. 1283.) It was enacted as Public No. 381, 74th Congress, August 27, 1935.

President Roosevelt in his message to Congress of June 7, 1935, stated in part:

> "It is high time to deal with the Nation's transportation as a single, unified problem. * * * In the railroad field there has been a growing recognition of the necessity for reorganization and coordination. * * * To enable necessary financial reorganizations to be effected inexpensively and promptly the Congress passed, two years ago, certain amendments to the Federal Bankruptcy Act. Shortcomings in this legislation have appeared which have prevented an efficient and extensive use of it. In order to correct these shortcomings the Coordinator has recommended certain amendments which are now before the Congress for action. Various differences of opinion as to these amendments are rapidly being adjusted and it is my hope that this legislation may be promptly enacted." (79 Cong. Record 8851)

Senator Wheeler, as Chairman of the Committee on Interstate Commerce, in introducing the 1935 amendments to Section 77, stated that that statute "was an attempt to get away from the inefficient and expensive equity reorganizations, the maladministration of which had been notorious" by bringing "the Interstate Commerce Commission into active development of plans, enabling a proper consideration of the public interest and the development of reorganizations according to a common pattern. * * * The law must be effective for such reorganizations as the country has never seen before." (79 Cong. Record 13764)

Events confirmed this prediction. In reviewing the situation in 1938, the Commission found that "railroad bankruptcy has risen to a point never before reached in this country."[1] In its 54th Annual Report to Congress dated November 1, 1940, the Commission stated:

> "On July 31, 1940, the number of steam railways in receivership or trusteeship was 107. They accounted

[1] *Fifteen Percent Case*, 1937-1938, 226 I. C. C. 41, 59.

> for 76,989 miles of road operated, or 31.04 percent of the entire railroad mileage. . . . The unfavorable financial condition of the railways as a whole in recent years has attracted widespread attention." (p. 27)

This statement, dealing with the railroad mileage of the United States as a whole, falls far short of showing the extent of the financial disaster which befell the roads operating in the western trunk line territory, in which a large portion of the mileage of the debtor is located. Other western trunk line carriers which are in the hands of the court or have just been released are the Missouri Pacific, the Wabash, the North Western, the Chicago Great Western, the Soo, the Rock Island, the Minneapolis & St. Louis, the Chicago & Eastern Illinois, the Wisconsin Central and the Monon. Of the major roads having their principal mileage in western trunk line territory only the Burlington has thus far escaped bankruptcy.

These widespread railroad bankruptcies which, by the enactment of Section 77, Congress sought to enable the Commission to handle effectively, are the culmination of adverse factors in the railroad industry which have been operating inexorably and with increasing severity for many years. The distressing decline in the financial position of the railroads was disastrously aggravated by the inroads during the past fifteen or twenty years of new competitive agencies in the transportation field, notably highway motor vehicles, inland waterways, pipe lines and air transportation.[2] The adverse effect of these new competitive agencies upon the traffic and rate structure of the railroads has increased progressively and in alarming proportions.

Confronted with these grave economic conditions which menaced the solvency of the entire railroad industry, and particularly those railroads serving the great agricultural

[1] *Revenues in Western District, Ex Parte 87*, 113 I. C. C. 3, 37.

[2] *See 1931 Fifteen Percent Case, Ex Parte 103*, 178 I. C. C. 539, 573-5.

areas of the middle west, Congress, in the thoroughgoing amendments of 1935, placed upon the Commission the larger duty and authority to prescribe a plan of reorganization which could be made effective in the public interest even in the absence of assent thereto by particular classes of creditors. In the light of the specific issue here it should be emphasized that the 1935 amendments also lodge in the Commission the power to determine value, when necessary, and require that any valuation be "based upon capacity to earn, rather than upon the original investment or a hypothetical reproduction cost."[1] Many other charges designed to make Section 77 more effective in the prompt reorganization of interstate railroads were introduced by the 1935 amendments. The newly created position of the Commission in the reorganization process was emphasized throughout and the court was required to remand to the Commission for further action a plan certified by the Commission in the event that the court did not approve it.

This Court has found that, while Congress did not completely withdraw all control of railroad reorganization from the courts, a step for which it states there was strong sentiment, no doubt was left that the Commission was the agency entrusted with the evolution of the plan of reorganization and that "Congress did not mean to grant to the district courts the same scope as to bankrupt roads that they have in dealing with other bankrupt estates." In *Palmer* v. *Massachusetts*, 308 U. S. 79, 86-87 (1939), this Court stated:

"Until the amendment of March 3, 1933, railroads

[1] Report of the Committee on Interstate Commerce of the Senate dated July 29, 1935, recommending the passage of the 1935 amendments, S. Rep. No. 1336, 74th Congress, 1st Session, p. 3. Senator Wheeler, as Chairman of the Committee on Interstate Commerce, in introducing the 1935 amendments stated that valuation hearings which were thus to be avoided under the amendments "are almost without any equal in jurisprudence for size and expense." (79 Cong. Record 13764)

were outside the Bankruptcy Act. But the long history of federal railroad receiverships, with the conflicts they frequently engendered between the federal courts and the public, left an enduring conviction that a railroad was not like an ordinary insolvent estate.[1] Also an insolvent railroad, it was realized, required the oversight of agencies specially charged with the public interest represented by the transportation system. Indeed, when, in the depth of the depression, legislation was deemed urgent to meet the grave crisis confronting the railroads, there was a strong sentiment in Congress to withdraw from the courts control over insolvent railroads and lodge it with the Interstate Commerce Commission. Congress stopped short of this remedy. But the whole scheme of § 77 leaves no doubt that Congress did not mean to grant to the district courts the same scope as to bankrupt roads that they may have in dealing with other bankrupt estates:

"The judicial process in bankruptcy proceedings under § 77 is, as it were, brigaded with the administrative process of the Commission. From the requirement of ratification by the Commission of the trustees appointed by the court to the Commission's approval of the court's plan of reorganization the authority of the court is intertwined with that of the Commission."

In its first decision in a case arising under Section 77, *Continental Bank* v. *Rock Island Ry.*, 294 U. S. 648 (1935), this Court stated:

"Section 77 advances another step in the direction

[1] In its footnote to this statement the Court referred, among other things, to "Chapter XXII 'Railroad Receiverships' in * * * 'The Life of Walter Quintin Gresham', pp. 366-378", which recounts the experiences of Walter Q. Gresham as District Judge of Indiana and those of Circuit Judge Thomas Drummond of the Seventh Circuit, in their handling of certain railroad receiverships around 1870. Many of the earlier developments in railroad reorganizations, including the displacement of mortgage liens in favor of operating and wage claims, are shown to have been based on the view expressed by Judge Drummond in entering an order in the reorganization of the Indianapolis, Bloomington & Western R. R. Co. in 1878 that: "A railroad mortgage is not like an ordinary mortgage on a farm or a house. A railway is a matter of public concern." (p. 377; cited in 308 U. S. at page 86, footnote 12)

of liberalizing the law on the subject of bankruptcies. * * * A railway is a unit; it can not be divided up and disposed of piecemeal like a stock of goods. It must be sold, if sold at all, as a unit and as a going concern. Its activities can not be halted because its continuous, uninterrupted operation is necessary in the public interest; and, for the preservation of that interest, as well as for the protection of the various private interests involved, reorganization was evidently regarded as the most feasible solution whenever the corporation had become 'insolvent or unable to meet its debts as they mature.' * * * A proceeding under § 77 is not an ordinary proceeding in bankruptcy. It is a special proceeding which seeks only to bring about a reorganization, if a satisfactory plan to that end can be devised. And to prevent the attainment of that object is to defeat the very end the accomplishment of which was the sole aim of the section, and thereby to render its provisions futile." (pp. 671, 676)

(b) The Commission's Plan as Approved by the District Court Effectuates the Congressional Intent, While the Decision of the Circuit Court of Appeals Would Nullify This New Legislation.

In the present reorganization proceedings the Interstate Commerce Commission conducted a long and painstaking investigation. There were numerous hearings at which all interested parties were given the fullest opportunity to present evidence and to examine and cross-examine witnesses. Through its Bureaus of Valuation, Finance and Accounts, the Commission made its own studies of various phases of the problem, the results of which were made a part of the record, subject to scrutiny, examination and rebuttal. On such a record, and after hearing all parties on brief and in argument, the Commission prescribed a plan of reorganization which it supported by extensive findings in its original report and supplemental report. Appropriate orders accompanied both the original and supplemental reports as they were certified to the District Court.

The District Court, on the objections of the trustees of certain of the mortgages and other interests and representations of the stockholders, reviewed the Commission's plan. It held hearings over a period of eight days, during which it received much evidence tendered by the objectors to the plan. Thereupon, on the basis of such evidence and the evidence before the Commission, it approved the plan as fair and equitable under the provisions of Section 77. The District Court filed its opinion (R. 1857-1899) which it followed with findings of fact, conclusions of law, and an order approving the plan. (R. 1978-1992)

The Circuit Court of Appeals reversed the order of the District Court and remanded the proceedings to the Commission on the sole ground that the reports and orders of the Commission were inadequate in respect to findings necessary to support the plan. The court declared that, while in its opinion the evidence of record was adequate to support the plan, it interpreted this Court's decision in *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510, a case dealing with a non-railroad reorganization, as requiring other and additional findings, different from those made by the Commission, in order to permit a reviewing court to give its approval to the Commission's plan. We believe that the court thus failed to give the statute the interpretation necessary to its practical administration, and in so doing would render it ineffective in dealing with the problems for the solution of which it was specially designed.

Congress had plainly defined the kind of report which it intended the Commission to make as one in which "the Commission shall state fully the reasons for its conclusions." (Section 77(d)) The Commission fully complied with that direction. The court did not discuss the adequacy of the report in relation to this definitive requirement in the Section respecting the form of the report and in fact it made no reference to the provision.

We review later in this brief the comprehensive findings embodied in the Commission's reports to show that they would fully meet the requirements which this Court has laid down in respect to "an ordinary insolvent estate"[1] like that undergoing reorganization in the *Consolidated Rock Products* case. But we submit that the intent and purpose of Section 77 and its requirements, as stated by Congress, lay no such burdens upon the Commission acting as an administrative agency of the Government as would be imposed by the ruling of the Circuit Court of Appeals.

The decision of the Circuit Court of Appeals in effect holds that Congress, confronted with the necessity of providing machinery for an expedited method of railroad reorganization in which the public interest would be paramount, merely set up an additional tribunal, the validity of whose determination would be gauged by the District Court on the basis of specific and detailed findings in the same way in which the District Court in an equity reorganization would have determined the validity of a plan presented by reorganization managers. In effect, therefore, the Circuit Court of Appeals not only would deprive the Commission's determination of the dominant characteristics with which Congress intended to invest it, but would also deprive the determination underlying the District Court's approval of the plan, of any real legal significance. The Commission's decision would thus be deprived of the usual attributes of its decisions on matters other than railroad reorganization, and the Commission, with its expert knowledge on technical matters, relegated to the position of an additional inferior tribunal, having the function of a mere fact-finding agency. This Court has recently held:

> "It is not the province of a court to absorb the administrative functions to such an extent that the executive or legislative agencies become mere fact-finding

[1] *Palmer* v. *Massachusetts*, 308 U. S. 79, 86 (1939).

bodies deprived of the advantages of prompt and definite action." *Gray* v. *Powell*, 314 U. S. 402, 412 (1941).

The decision of the Circuit Court of Appeals ignores the basic differences in origin and function between courts and administrative tribunals, often pointed out by this Court. In *Federal Communications Commission* v. *Pottsville Broadcasting Co.*, 309 U. S. 134, 143-4 (1940) the Court said:

> "These differences in origin and function preclude wholesale transplantation of the rules of procedure, trial, and review which have evolved from the history and experience of courts. Thus, this Court has recognized that bodies like the Interstate Commerce Commission, into whose mould Congress has cast more recent administrative agencies, 'should not be too narrowly constrained by technical rules as to the admissibility of proof,' *Interstate Commerce Commission* v. *Baird*, 194 U. S. 25, 44, should be free to fashion their own rules of procedure and to pursue methods of inquiry capable of permitting them to discharge their multitudinous duties. * * * They require that interested parties be afforded an opportunity for hearing and that judgment must express a reasoned conclusion. But to assimilate the relation of these administrative bodies and the courts to the relationship between lower and upper courts is to disregard the origin and purposes of the movement for administrative regulation and at the same time to disregard the traditional scope, however far-reaching, of the judicial process. Unless these vital differentiations between the functions of judicial and administrative tribunals are observed, courts will stray outside their province and read the laws of Congress through the distorting lenses of inapplicable legal doctrine." (pp. 143-4)

The decision of the Circuit Court of Appeals also completely overlooks the fact that Congress conferred on the District Court the power of determining whether the plan certified by the Commission should be sustained and the

duty, which the District Court fulfilled, of approving the plan for submission to the creditors if it determined that the plan should be sustained.[1]

II.

THE PLAN FULLY COMPLIES WITH THE REQUIREMENTS OF SECTION 77.

(a) Requirements of the Statute.

The authority of the Commission in respect to the formulation of a plan of reorganization is definite and precise:

> "After the filing of such a plan [by the debtor], the Commission, unless such plan shall be considered by it to be *prima facie* impracticable, shall, after due notice to all stockholders and creditors given in such manner as it shall determine, hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subsections (b) and (e) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. In such report the Commission shall state fully the reasons for its conclusions." (Section 77, subsection (d))

Subsections (b) and (e), therein referred to, are set forth in the appendix to this brief. Subsection (b) provides the essential requirements of a plan of reorganization to be certified by the Commission, and subsection (e) provides for hearings by the District Court upon a certified plan and approval by the judge when satisfied that the stated requirements have been complied with.

[1] See pp. 17 and 18 of this brief.

Section 77, subsection (c) (11), also set forth in the appendix to this brief, provides for the use by the Commission of its various agencies in compiling for introduction in evidence, necessary studies concerning the property, business, earnings, corporate organization and similar matters to assist the Commission in the preparation of a plan of reorganization.

The plan which the Commission certified to the District Court together with its report stating "fully the reasons for its conclusions", and which the District Court approved, was a plan that differed markedly from that proposed by any party to the proceeding. The Commission declared that the public interest was paramount and that its endeavor was "to devise a plan that will serve as a basis for the company's financial structure for the indefinite future." (R. 2220) While the debtor and some of the other parties pressed upon the Commission their requests for indefinite postponement of the reorganization proceedings, the Commission declined to grant them, saying:

> "It is true that the plan will involve sacrifices on the part of the bondholders. But refusal by us to approve any plan until present uncertainties are resolved and the earning power of the system is stabilized would be to delay the reorganization indefinitely. None of the parties has attempted to predict a time or describe the conditions when the making of a plan would be considered proper. This proceeding has been pending for more than four years, and, under any circumstances, cannot be concluded in the immediate future. Further postponement cannot remove the limitations upon allowable fixed charges imposed by the record of past earnings." (R. 2220)

(b) Plans of Reorganization as Presented by the Parties and the Plan Approved by the Commission.

From this background and with a purpose to certify a plan which would conform to the letter and the spirit of the

law, the Commission gave its approval to a plan which, in the language of the statute, was "different from any which has been proposed." (Section 77(d)) Three plans were filed with the Commission. These were, the debtor's original plan, the plan of the Group of Institutional Investors, and the plan incorporating the debtor's suggested modifications to the Group of Institutional Investors' plan.

The debtor's petition for reorganization, alleging its inability to meet its debts as they matured, presented a proposed plan of reorganization dated July 1, 1935. (R. 5-42) At the first set of hearings before the Commission on August 5, 6, and 7, 1935, the debtor presented evidence in support of that plan, which became known as the "stand-by plan". It is described by the Commission in its report (R. 2182-2187), the principal features being:

(a) Extension of debt due Reconstruction Finance Corporation for ten years, with provision for borrowing an additional $12,000,000;

(b) Provision that one-third of the interest on General Mortgage bonds should become contingent upon earnings for ten years and fully cumulative, with the other two-thirds of the interest on such bonds remaining fixed;

(c) Provision making all interest on Fifty Year Five Per Cent. Mortgage bonds, and all interest on Chicago, Milwaukee & Gary bonds contingent upon earnings, but cumulative and with the right in the holders to declare principal and unpaid interest due if the accumulation should aggregate ten years' interest;

(d) Provision for exchanging Convertible Adjustment Mortgage bonds with accruals of unpaid interest for new preferred stock; and

(e) Provision for exchange of preferred stock, share for share, for new common stock with $25 par value, and

exchange of each share of common stock for one-third share of new common stock.

Representatives of certain creditor interests, including the Group of Institutional Investors, expressed approval of this plan, as a stand-by arrangement, at the hearing on August 7, 1935, provided it could be approved and made effective promptly. (R. 536) The Reconstruction Finance Corporation also conditionally approved the plan, including the making of the additional loan, but later canceled its commitment. (R. 2182) This plan was not approved and the Commission proceeded with its investigation. When the matter was again set for hearing in June, 1937, the debtor presented a report of a Special Committee of its Board of Directors, whose members testified that the debtor's plan was no longer feasible. (R. 586-592) They stressed two major defects which had become evident in any such stand-by arrangement as that contemplated by the 1935 plan, viz.: the inadequacy of its provisions for future financing, and the provision respecting cumulative contingent interest for the Fifty Year Five Per Cent. Mortgage bonds. It was contended that in the face of the uncertainties as to the general business conditions, wages, prices and rates then existing, it was impossible to recommend either a modification of the 1935 plan or a new plan. (R. 587, 589)

Debtor thereafter petitioned for an indefinite postponement of the further hearings set by the Commission for September 20, 1937, which petition was denied. (R. 635) At that hearing debtor again stressed the uncertainties of railroad operations and the alleged defects in the plan, seeking a further adjournment. This request was denied and the hearings were closed. (R. 691) Thereafter, upon petition of the Group of Institutional Investors, the proceeding was reopened for the purpose of permitting that group or other parties who might desire to do so, to file proposed plans of reorganization by January 10, 1938.

(R. 692) The Group of Institutional Investors filed a plan on January 10, 1938. (R. 717, 2188; Com. Ex. 175) Hearings were held on February 1, 2, 3 and 4, 1938, and on March 21 and 22, 1938, at which time the record was closed.

Meanwhile, the debtor had presented its suggested modifications to the plan of the Group of Institutional Investors. (R. 2200-2206) It finally incorporated these suggested modifications "in the form of a complete plan" which it submitted to the Commission. (R. 2205; Com. Ex. 189)

The plan of reorganization certified by the Commission on June 4, 1940, and approved by the District Court on November 13, 1940, did not constitute an adoption of any of these plans, but represented the Commission's own determination of a plan "compatible with the public interest" and which, in its opinion, would be "fair and equitable, afford due recognition to the rights of each class of creditors and stockholders, and conform to the requirements of the law of the land regarding participation of such creditors and stockholders." (R. 2218)

(c) Changes in Plan Sought by Objectors Challenge the Determination of the Commission and the District Court on Matters Within Their Respective Jurisdictions.

This plan has been described.[1] The essential criticisms leveled at the plan by the several parties to the proceeding may be broadly summarized as follows: (1) Objections of the debtor and the committee representing the preferred stockholders of the old company to the finding that the equity of the stockholders was without value; and that they should not participate in the distribution of the securities of the reorganized company; (2) objections of various classes of creditor interests that the new securities which the plan would allot to the members of the class were less in quantity and poorer in quality than they should receive, and that other classes were allotted more or better securities than they should receive.

[1] See pp. 11-15 of this brief.

Practically every controversy before the Commission, in the District Court and in the Circuit Court of Appeals resulted from the Commission's determination to reduce the capitalization and fixed and contingent interest charges thereunder in a measure consistent with the protection of the public interest; its determination to provide a simplified capital structure and an essential additions and betterments fund, also in the public interest; and its effort to provide an equitable distribution of the new securities which resulted from the capital structure thus approved, thus effectuating a reorganization in the public interest.

The debtor's excessively complicated capital structure, and the desirability in the public interest of creating a new structure with only two layers of system mortgages, coupled with the decline in the earning power of the system, made the problem difficult and peculiarly one for determination by the administrative tribunal which had been regulating this and other railroads for more than half a century. In its report the Commission said:

> "Due to the comparatively low income which the system can fairly be depended upon to earn for the payment of interest and for other corporate purposes in the future, the fixed-interest charges of the system must be reduced to a point that results in a substantial reduction of the principal amount of fixed-interest obligations. Income bonds and securities junior thereto must, to a large extent, replace existing fixed-interest bonds." (R. 2214-2215)

As to the Commission's effort to substitute a simplified capital structure and to provide equitably for the issuance to creditors of new securities in the amounts and upon the terms set forth in the plan (Section 77(b)), the District Court declared:

> "The plan of distribution followed by the Commission would seem to be in accord with sound principle and should have judicial approval. • • • The advantage resulting from the elimination of divisional

mortgages is obvious. In fact, many of the difficulties arising in current reorganization proceedings are attributable in large measure to the existence of many mortgages on parts of a system. The desire of the Commission to eliminate that objection is commendable." (R. 1888)

The nature and extent of the Commission's findings and conclusions, as stated in its reports, on the many issues in controversy during the protracted proceedings before it, and the disposition which the District Court, after hearing, made of each of the several specific objections to the plan filed with it pursuant to the statute (Sec. 77(e)), are discussed in the next section of this brief. In passing upon these objections, the District Court exercised an independent judgment on every feature of the plan to which objection was made, and upon the plan as a whole, and thus fully discharged the duties laid upon it under subsection (e) quoted above. In construing the statute, it referred to the decision of this Court in *Warren* v. *Palmer*, 310 U. S. 132 (1940), and said:

> "That Court has not yet determined just what weight should be given by the Court to the findings and conclusions of the Commission. Clearly, the Court has power to correct errors of law into which the Commission may have fallen and to set aside findings of fact which are not supported by the record or conclusions which violate constitutional rights. On the other hand, the initial determination of the questions bearing upon the soundness and reasonableness of a Plan of Reorganization is the responsibility of the Commission which is peculiarly fitted for the consideration of such questions and *its findings and conclusions, made and reached after extended hearings and exhaustive study, as in this case, should be given great weight.*
>
> "In these cases, the amount and character of the capitalization of the reorganized company, the fixed charges, and the distribution of new securities are all questions of prime importance, and their determination affects the public interest.

"With these principles in mind, let us consider the objections which have been presented to this Plan." (R. 1870)

The history of the statute and the decisions of this Court leave no doubt that the District Court was on sound ground in giving "great weight" to the findings and conclusions of the Commission.

Section 20a of the Interstate Commerce Act, which gave the Commission sufficient control over the issuance of securities by solvent roads, had proved inadequate, in practical operation, in respect to properties undergoing reorganization, as shown by the financial history of this very property. By that Section of the Transportation Act of 1920 Congress had committed to the Commission exclusive jurisdiction over the issue of securities by common carriers, and had provided that the Commission should approve only such securities as were "compatible with the public interest." (49 U. S. C. A., Sec. 20a) This Court has held that the term "public interest," as used in the Transportation Act of 1920, has "direct relation to adequacy of transportation service, to its essential conditions of economy and efficiency, and to appropriate provision and best use of transportation facilities, questions to which the Interstate Commerce Commission has constantly addressed itself in the exercise of the authority conferred." *New York Central Securities Corporation* v. *United States*, 287 U. S. 12, 25 (1932).

The meaning of the requirement of Section 20a of the Transportation Act of 1920, in respect of railroad reorganizations, was stated by the Commission in the *Denver & Rio Grande Western Reorganization*, 90 I. C. C. 141 (1924), as follows at page 148:

"The public interests require that, before an issue of securities by a carrier is authorized, the probability of earnings sufficient to pay costs of operation and of fixed charges be reasonably established, with some surplus for dividends and other purposes."

The Commission and the Congress were to learn, however, as emphasized so strikingly by the vicissitudes of this road, that in practice it was not possible to give effect to the protective principles underlying Section 20a with respect to the issuance of securities in reorganization proceedings. In *Investigation of Chicago, Milwaukee & St. Paul Railway Company* (131 I. C. C. 615) and in *Chicago, Milwaukee & St. Paul Reorganization* (131 I. C. C. 673) the Commission asserted that the capital structure then proposed for the reorganized company had obvious shortcomings, and was manifestly defective. (p. 694) Nevertheless it felt impelled to approve the issuance of new securities rather than to void a plan as it had been evolved through the long processes of an equity receivership. The Commission declared such a situation to be one which "is fundamentally unsatisfactory and requires reform." (p. 671)

In enacting Section 77, Congress thus had in mind that the duty which Congress had imposed upon the Commission by Section 20a to "veto the entire reorganization," if it found the issuance of securities in a railroad reorganization not to be "compatible with the public interest," had placed the Commission "in a most embarrassing and difficult position, because its authority (under Section 20a) is not sought until every other step has been taken."[1] The correction of this "fundamentally unsatisfactory" situation in railroad reorganization proceedings was one of the primary objectives of Congress in enacting Section 77. To invalidate the Commission's plan would violate Section 77 and impair the powers of both the Commission and the District Court thereunder.

[1] Page 7 of letter dated January 31, 1933, from Legislative Committee of Interstate Commerce Commission in reply to Honorable Daniel O. Hastings, Chairman of Subcommittee of the Judiciary Committee of the United States Senate respecting Section 77.

III.

IN DISCHARGING ITS DUTIES UNDER SECTION 77, THE COMMISSION SUPPORTED THE CERTIFIED PLAN BY REPORTS CONTAINING COMPREHENSIVE FINDINGS AND CONCLUSIONS.

(a) The Commission Stated Its Findings in the Same Form That Has Repeatedly Been Determined by This Court to Be Adequate and Lawful.

As noted, Section 77 requires that in its report approving a plan, "the Commission shall state fully the reasons for its conclusions." (Subsection (d)) Congress enacted this provision in the light of the repeated and then recently expressed views of this Court as to the nature, form and extent of findings by the Commission requisite to sustain its orders.

In sustaining findings of administrative bodies against attacks for lack of formalism, this Court time and again has declared that such findings must be given a practical application and interpretation. Two of the first and most important controversies involving the Transportation Act of 1920 to reach this Court were the *New England Divisions Case*, 261 U. S. 184 (1923), and *Colorado v. United States*, 271 U. S. 153 (1926). That statute replaced an incomplete regulatory power of the Commission with broad and plenary power just as did Section 77 in the following decade with regard to railroad reorganizations.[1] In the first case the Court, in upholding the Commission's order as to the division of joint through rates under the provisions of the Transportation Act of 1920 against attack on the "method of proof and of adjudication pursued," held that:

---

[1] See Jacobs, The Interstate Commerce Commission and Interstate Railroad Reorganizations, 45 Harv. L. Rev. 855, 863.

"Obviously, Congress intended that a method should be pursued by which the task, which it imposed upon the Commission, could be performed." (261 U. S. 184, 197)

Similarly, in the second case the Court refused to enjoin an order of the Commission permitting the abandonment of a branch line in Colorado under the provisions of the Transportation Act of 1920. It was contended, in the words of the Court "that the order is void, so far as it relates to intra-state traffic, because essential findings were not made and, also, because essential findings made were not supported by evidence." (271 U. S. at p. 166) This Court rejected such a contention and refused to impose impractical requirements as to findings, saying at page 169:

"An examination of the extensive record and of the three opinions of the Commission convinces us that no relevant fact was ignored, that there was ample evidence to support the facts found * * *."

In subsequent cases, the Court has repeatedly restated this view. The same constructive attitude toward findings of fact by the Commission is well shown in several railroad rate cases. In *United States* v. *Louisiana*, 290 U. S. 70 (1933), the Court said:

"It cannot be supposed that Congress, in placing this duty on the Commission, intended, in the absence of some express provision compelling it, that the Commission should follow a procedure which would preclude its acting effectively, if at all. That such was not its intention appears from the words of the statute. It does not, in terms, command the Commission to find that each rate prescribed under § 15a is just and reasonable, as prerequisite to a general increase in rates." (p. 76)

"* * * The administrative difficulties which would preclude performance of the duty imposed by § 15a if the Commission were required to find that each individual rate prescribed is just and reasonable, would similarly prevent compliance with that under § 13(4). Since neither can be performed effectively without per-

> formance of the other, the standard of reasonableness to which the Commission must conform is necessarily the same under both, and that implies that under § 13(4), as under § 15a(2), reasonable latitude must be given for modification of particular rates found to be unreasonable." (pp. 78-79)

Challenge was also made in that case that the Commission had not found that revenues would be increased by the change in rates. The Court examined the entire opinion of the Commission and, while not commending its form, found that, taken as a whole, the report showed

> "* * * the conclusion of the Commission, based upon supporting data, including estimates of experienced railroad traffic men, to which the report refers, that the probability of increased revenue was sufficiently great to make the increase of rates a reasonable exercise of sound managerial judgment. This, we think, meets the requirements of the statute."[1] (p. 80)

In *Florida* v. *United States*, 292 U. S. 1 (1934) the order of the Commission there in question was supported by findings and evidence which the Court held to be sufficient. As to the findings, it answered the appellant's objections with words substantially applicable here:

---

[1] As to the form of the Commission's findings this Court stated the rule in *United States* v. *Baltimore & O. R. Co.*, 293 U. S. 454, 464 (1935) as follows: "In the *Florida* case (*Florida* v. *United States*, 282 U. S. 194) the legal distinction was pointed out between what may be termed quasi-jurisdictional findings, there held to be indispensable, and the 'complete statement of the grounds of the Commission's determination' which was declared in *Beaumont, S. L. & W. Ry. Co.* v. *United States*, 282 U. S. 74, 86, to be desirable for a proper consideration of the case in the courts. The lack of such a complete statement, while always regrettable, because unnecessarily increasing the labor of the reviewing court (compare *Virginian Ry. Co.* v. *United States*, 272 U. S. 658, 675), is not fatal to the validity of the order." Similarly in *Meeker and Co.* v. *Lehigh Valley R. R.*, 236 U. S. 412, 428 (1915) this Court said of a report of the Commission: "True, the findings in the original report are interwoven with other matters and are not expressed in the terms which courts generally employ in special findings of fact, but there is no difficulty in separating the findings from the other matter or in fully understanding them."

"The requirement of essential findings as to revenues did not demand an impracticable exactness. Losses through inadequate rates could be shown satisfactorily even though proof of the precise extent of such losses was not available. Reasonable determinations were required and these were made." (p. 9)

In all of these cases this Court required such findings as the conditions reasonably warranted and permitted, and interpreted that requirement in a practical manner consistent with the realities and the intent of the law to effectuate the administrative process. Compare also, Stone and Black, JJ., dissenting in *Interstate Circuit, Inc.* v. *U. S.*, 304 U. S. 55, 58 (1938). We submit that the action taken by the Commission in this case, judged in the same spirit, is entirely valid.

Here, as in *United States* v. *Louisiana, supra*, "It cannot be supposed that Congress * * * intended * * * that the Commission should follow a procedure which would preclude its acting effectively, if at all." (p. 76) Indeed Congress made possible effective and practical action by the Commission in regard to findings by providing that in its report approving the plan the Commission "shall state fully the reasons for its conclusions." (Section 77(d)) These are words of art so chosen as to avoid impracticable requirements in regard to findings. Section 14 of the Interstate Commerce Act had originally provided that the Commission's report should "include the findings of fact upon which the conclusions of the Commission are based." (Act of Feb. 4, 1887, 24 Stat. 384) In 1906, this section of the Interstate Commerce Act was amended to provide that "whenever any investigation shall be made by said Commission, it shall be its duty to make a report in writing with respect thereto, which shall state the conclusions of the Commission together with its decision, order, or requirement in the premises; * * *." (Act of June 29, 1906; 34 Stat. 589) The words of this amended statute, under which there had been held to be "no formal requirements for the findings to be made by

the Commission,'"[1] were selected by Congress for use in subsection (d) of Section 77.

The only reference anywhere in Section 77 to a "finding" is in the provision of subsection (e) that "submission" [of the plan] to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, * * * that at the time of the finding the equity of such class of stockholders has no value," and that "submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, * * * that at the time of the finding the interests of such class of creditors have no value." The Commission fully complied with these requirements.[2]

In spite of this clear enunciation of what would be required of the Commission by way of findings to permit the courts to sustain its conclusions, in the light of which Congress enacted Section 77 in 1933, and the amendments thereto in 1935, the Circuit Court of Appeals reversed the District Court, not for any deficiency of evidence, which was held sufficient to sustain the plan, but solely because of alleged inadequacy of findings.

In certifying this plan of reorganization to the District Court, the Commission was most scrupulous in its endeavor to accord fair and equitable treatment to every interest, but in doing so it did not undertake to state in terms of dollar values the collateral and railroad property securing each of the numerous mortgages. It is doubtful whether in the case of a highly complicated corporate structure of the magnitude of that of a major railroad system such

[1] *United States* v. *Louisiana*, 290 U. S. 70, 80 (1933)

[2] The plan did not provide for submission to either the preferred or common stockholders of the debtor, since, as herein stated, the Commission found that the equity of such classes of stockholders has no value (R. 1341, 2260) and the judge, the District Court, affirmed that finding. (R. 1991) The Circuit Court of Appeals approved the finding by the Commission and its affirmation by the District Court. (R. 2311, 2335)

findings could be made within any reasonable period of time or in any such form as would be of practical value to the reorganization process. We have referred to the declaration of this Court that "Congress intended that a method should be pursued by which a task, which is imposed upon the Commission, could be performed."[1] In enacting Section 77, Congress well knew that the most difficult and time consuming undertaking ever imposed on the Interstate Commerce Commission had been its work under the Valuation Act of 1913, which directed the Commission to make valuations of the railroads. (49 U. S. C. A., Sec. 19a) Sharfman, in his treatise, *The Interstate Commerce Commission*, states, for example, that "the magnitude and difficulty of the undertaking are clearly evidenced by the fact that the valuation work, begun in 1913, was, in 1930, still incomplete." (Vol. I, pp. 118-119) In the enactment of Section 77 as amended in 1935, it was the purpose of Congress to avoid such valuation proceedings which were recognized to be "almost without any equal in jurisprudence for size and expense."[2] The tremendous task of determining single sum valuations not only for each railroad system as a whole, but for each of the many integrated mortgage divisions of a property which is operated as a single system, and then for each set of liens supporting each of the several mortgages, some of which have a first, second, third or fourth lien on various parts of debtor's system, would make the Act unworkable.

In sustaining the constitutionality of Section 77, this Court found that Congress intended to provide for the expeditious reorganization of bankrupt railroads by avoiding the delays incident to the receivership practice.

---

[1] *New England Divisions Case*, 261 U. S. 184, 193 (1923).

[2] See legislative history of Section 77 in the footnote on p. 27 of this brief and also the statement of the Committee on Interstate Commerce of the Senate that the last paragraph of subsection (e) was proposed as part of the 1935 amendments to Section 77 "in order to eliminate the great expense of valuation hearings." (S. Rep. No. 1336, 74th Congress, 1st Session, p. 3)

In *Continental Bank* v. *Rock Island R. Co.*, 294 U. S. 648, the Court said:

> "The delay and expense incident to railroad receiverships and foreclosure sales constituted, probably, the chief reasons which induced the passage of § 77; and to permit the perpetuation of either of these evils under this new legislation would be subversive of the spirit in which it was conceived and adopted." (p. 685)

Certainly it cannot be doubted that to require the Commission to enter upon the tortuous task of determining the single sum value in dollars and cents of the security back of each of the debtor's many mortgages, as well as to determine the single sum value of the new securities to be issued under the plan would open the door to interminable delay and litigation.

On the comprehensive record before it, including extensive studies by its own staff, the Commission could and did form the judgments necessary to a fair and equitable allocation of the new securities. It did not attempt to compile a catalogue of single sum, dollars and cents, values, and thus avoided an effort which could have been designed only to clothe its findings with the form and pretense of a precision which of necessity could not be attained in fact.[1] The Commission did, however, "fully state the reasons for

[1] This was recognized by the Commission in its recent report approving a plan of reorganization for St. Louis Southwestern Ry. (252 I. C. C. 325 (1942)) in which it stated: "The properties comprise one operating unit; a complete separation of values would necessarily have to be based on extensive assumptions of unprovable validity; and any attempt at such a separation would in the end serve no purpose except to present an apparent certainty in the formulation of the plan which does not exist in fact. The Act calls for valuations only where necessary; and in our view further valuations are not necessary here." (p. 361) Compare the statement of this Court in *Continental Bank* v. *Rock Island Ry.*, 294 U. S. 648, 671 that "A railway is a unit; it can not be divided up and disposed of piecemeal like a stock of goods." (This brief, pp. 28-29) See also *N., C. & St. L. Ry.* v. *Browning*, 310 U. S. 362, 370 (1940), in which this Court said: "* * * railroads, unlike farms and city lots and stocks and bonds, are not objects of exchange. The very notion of a 'full cash value' for a railroad is in many respects artificial."

its conclusions" (Sec. 77(d)) and made all findings essential to the support of those conclusions. We shall now point out the nature of these findings which the Commission did make, with appropriate record reference to its original and supplemental reports.

(b) Findings as to the Debtor's Property as a Whole.

1. DETERMINATION OF AMOUNT AND CHARACTER OF NEW SECURITIES AVAILABLE FOR DISTRIBUTION.

The development of the Commission's plan involved two major steps. These were: (1) the determination of the total permissible capitalization and capital structure in the light of the public interest and the standards of value prescribed by the statute, and (2) the allocation of the new securities of the reorganized company among the creditors of the debtor.

The properties of the debtor were described at the outset of the Commission's original report. (R. 2162, *et seq.*) These properties were found to have an original cost of $694,263,606, cost of reproduction new, $818,280,465, cost of reproduction less depreciation, $546,341,054, value of lands and rights, $78,259,228, and working capital, $7,727,300. (R. 2164) Corresponding elements of physical value were found for each mortgage division and for the Terre Haute lines.

The Commission then turned to the earning power of the property and stated the results of the elaborate studies of the debtor's traffic, past, present and prospective, including the average annual tonnage of the various commodities for five separate periods in the years from 1921 through 1936, and the freight and total revenues for each year, 1927 through 1937. (R. 2176; 2177) It then considered the kinds of commodities the movement of which had recovered from the depression and the kinds in which the losses were most pronounced, and stated the passenger revenues and their trend over the period, 1921-1937 (R. 2177), and dis-

cussed the events leading to bankruptcy. (R. 2177-2178) Detailed findings were made as to the operating revenues and expenses in 1934, 1935, 1936, and 1937, and the estimates for 1938. (R. 2178, 2179) The physical condition of the property with reference to maintenance and efficiency of operation was carefully analyzed. (R. 2179) The income available for payment of interest in each of the years 1921 to 1938 was stated, both as reported by the carrier and as adjusted in the manner described by the Commission. (R. 2180, 2181) Careful consideration was given to the estimates of future taxes, the effect of emergency freight charges, and the reductions in wages and salaries paid by the debtor. (R. 2181) Later in the report, the Commission, on the basis of the foregoing factors, and after discussing certain proposals, made this finding as to the amount of fixed charges which could be borne by the reorganized company:

> "If fixed interest charges be limited to about $4,269,654 and the mandatory payment to the fund to $2,500,000 a year, the total, $6,769,654, would be covered about 1.16 times by the average earnings of the period 1931-35 and 1.18 times for the period 1932-36. In 1932, 1935, and 1938 such an amount was not earned. While 1939 shows an improvement in earning power, we would regard any increase in the foregoing charges as hazardous. Between the clear demands of a conservative policy in the present reorganization and the claims and rights of the first-lien bondholders, we conclude that the limitation of fixed charges of the system at approximately $4,269,654 a year is reasonable and proper. We find that there will be adequate coverage of such amount of fixed charges of the new company by the probable earnings available for the payment thereof." (R. 3219)

Determination of the permissible capitalization and capital structure also involved, among other things, (1) a detailed study of the corporate and financial structure of the debtor company and of the effects of its reorganization in the equity proceedings of 1925-1928 (R. 2165-2175), (2) de-

termination of the property subject to the various liens of the debtor's mortgages, the original cost thereof, and the cost of reproduction less depreciation (R. 2162 *et seq.*; I. C. C. Bureau of Valuation Report on Elements of Value), (3) careful consideration of the debtor's plan of 1935 (R. 2182-2187), (4) careful consideration of the plan filed by the Group of Institutional Investors (R. 2188-2200), (5) careful consideration of the debtor's suggested modifications of the Group's plan (R. 2200-2206), and (6) the positions taken by all other parties (R. 2207-2212), all weighed in the light of the public interest as determined by the Commission. The conclusion was as follows:

> "Considering the past and prospective earnings of the Debtor and all other relevant facts, and the public interest, we are of the opinion and find that the total capitalization of the new company should not exceed approximately $108,780,470 of fixed-interest debt, $115,257,480 of contingent-interest debt, $108,675,971, par value, of preferred stock, and 2,158,194 shares of common stock, having no-par value. Taking the common stock at $100 a share, the approximate maximum capitalization would thus be $548,533,321. Total fixed-interest charges will approximate $4,269,654, and total interest charges $9,489,134 per annum. Including the mandatory payment to the capital fund and a sinking fund for the retirement of bonds, the charges ahead of dividends on the new preferred stock will be about $12,532,528 per annum. Giving effect to full 5 per cent dividends on the preferred stock the charges ahead of dividends on the common will be about $17,966,326 per annum." (R. 2218-2219)

The findings of the Commission as to the debtor's property as a whole and the permissible participation therein are sufficient.[1] There was no requirement that the Commission explicitly label its findings as findings of value. Similarly, in *R. R. Commission* v. *P. G. & E. Co.*, 302 U. S. 388, 400 (1938), the State Commission's fixing of

[1] The District Court so held (R. 1872) and the Circuit Court of Appeals concurred therein. (R. 2310-2311, 2335)

a rate base was held to be a sufficient finding of fair value for the purpose there at issue, i. e., the fixing of reasonable rates. The Court there said:

> "The Commission specifically found what it considered to be the rate base. 39 Cal. R. Com., p. 76. The Commission found that rate base to be reasonable. *Id.*, p. 77, note. *The import of its opinion is that the rate base represented the Commission's conclusion as to the value which should be placed upon respondent's property for the purpose of fixing rates.* It was upon that valuation that the Commission distinctly ruled that the rates it established would 'assure the Company a fair return on its properties.'" (p. 400)

The principle underlying the decision of this Court in the case just cited was applied by the Circuit Court of Appeals for the Sixth Circuit in sustaining the District Court's approval of the Commission's plan of reorganization for the Akron, Canton & Youngstown Railway Company. The court there said:

> "There is implicit in the Commission's determination that the total capitalization of the debtors could not exceed $8,500,000.00, a finding of an ultimate fact that the fair market value of the capitalizable assets of the debtors was that sum and no more." (*Akron, Canton & Youngstown Ry. Co.* v. *Hagenbach*, 128 F. (2d) 932, 937 (C. C. A. 6th, 1942))

As the Act contemplates, the Commission based its determination of the capitalization and capital structure of the reorganized company primarily upon a consideration of the earnings which it found could reasonably be expected to service the new securities. The evidence supports its conclusions, as the courts below have found.

The report prescribes the permissible level of fixed charges (R. 2219) and states in detail the evidence and the reasoning which underlie the conclusion on that feature of the plan. The Commission found that the total charges ahead of dividends on the new preferred stock, including

therein the mandatory payment of $2,500,000 to the additions and betterments fund and the sinking fund of approximately $543,394 for the retirement of general mortgage bonds, must be limited to $12,532,528. (R. 1317, 2219) The Commission pointed out that the debtor's income available for interest during nine of the eighteen years immediately preceding the effective date of reorganization (1921-1938) exceeded this requirement, that the requirement was almost met in three other years, and that the average annual income available during the entire eighteen-year period, embracing both good years and bad years, was almost $3,000,000 in excess of the requirement, an amount which would have provided substantial dividends on the new preferred stock. (R. 2180) In seven of the nine years the earnings were sufficient to have permitted payment not only of full dividends at the rate of 5% on the new preferred stock but also substantial amounts on the new common stock. (R. 2180) The Commission found that these earnings warranted the allocation of new common stock to the Convertible Adjustment Mortgage bondholders for a portion of their claims, as follows:

> "As compared with the above-stated charges on the debt ahead of the adjustment mortgage bonds, the system income available for interest, as adjusted by the committee, averaged $21,038,461, a year during nine predepression years 1921-29. During the succeeding nine years, 1930-38, the average was $9,571,180, and during the entire 18 years it was $15,304,822. In the discussion of stockholders' equity which follows we take the position that the peak earnings of one or two years in the past cannot be relied on as indicative of an earning power sufficient for a finding that the equity is of value. In the case of the adjustment mortgage bonds the situation is different in that the charges on all prior-lien debt were more than covered over a long period of time prior to the depression and are nearly equalled by the average earnings during the past 18 years, as well as by the earnings predicted for the future normal year." (R. 2256)

In recognition of their prior rights the new fixed and contingent interest bonds and preferred stock are allotted exclusively to the holders of the old bonds which are senior to the Adjustments. To compensate these senior creditors further, and as fully as possible within the limitation imposed by the public interest in a simple and conservative capital structure, the plan provides certain valuable rights and characteristics for the new securities which they receive.

These senior bondholders who had no vote, much less control, in respect to the affairs of the present company, gain control of the reorganized property. During the difficult years immediately following reorganization, this control is assured by the voting trust. (R. 1344) After the expiration of the voting trust, the plan protects their control by providing that the new preferred stock (of which they are allotted 100%) shall

> "* * * be entitled, voting cumulatively as a class, to elect a majority of the board of directors of the new company until full 5 percent dividends shall have been paid upon the preferred stock, Series A, for three consecutive calendar years. Thereafter, each share of preferred stock, Series A, shall be entitled to vote equally with each share of common stock upon the election of directors, by cumulative voting, until such time as full dividends on the preferred stock, Series A, shall not have been paid during three consecutive calendar years, in which event the holders of the preferred stock, Series A, shall again become entitled to elect a majority of the board of directors and to retain this right until full dividends shall have again been paid for three consecutive calendar years, when equal voting rights for both classes of stock shall be resumed." (R. 1337-8)

Even if the earnings of the property shall be sufficient to permit continued payment of full dividends at the rate of 5% on the new preferred stock for more than three consecutive years, the plan makes it possible for these old

senior bondholders to continue their control of the reorganized company by providing that they may convert the series B general mortgage bonds which are allotted to them into new common stock at the rate of 10 shares of new common stock for each $1,000 bond, thus acquiring a total of 52% of the new stocks, both preferred and common.

In addition to control, other valuable rights are attached to both the new income bonds and the new preferred stock, which, as stated, are allotted exclusively to these old senior bondholders. A sinking fund is provided for both series A and series B general mortgage bonds amounting to ½% of the principal amount thereof annually, or approximately $543,394 (R. 1317, 1328); both series A and series B general mortgage bonds are made cumulative up to three years full interest requirements (R. 1327); and restrictions on the issuance and pledging of additional first mortgage bonds limit the new debt which can be placed ahead of the holders of new general mortgage bonds. (R. 1322, 1324, 1326) The new preferred stock, in addition to its 5% preferred dividend rate, is made participating with the new common stock, up to $1.00 per share, in dividends after $3.50 per share is paid on the new common stock (R. 1337); and no dividends can be paid on the new common stock unless and until full dividends at the rate of 5% have first been paid for three consecutive years on the new preferred stock. (R. 1337)

2. EXCLUSION OF THE OLD PREFERRED AND COMMON STOCKS.

The finding which excludes the old stockholders from the reorganized enterprise, is as follows:

> "We find that the equity of the holders of the debtor's preferred stock and its common stock has no value and the holders of claims in classes 24 and 25, therefore, are not entitled to participate in the plan." (R. 2260)

Such a finding is sufficient even apart from the specific provisions of Section 77. *In re 620 Church Street Building Corp.*, 299 U. S. 24 (1936)[1]; *R. R. Commission* v. *P. G. & E. Co.*, 302 U. S. 388 (1938). Moreover, it represents the determination by an expert tribunal of a matter peculiarly within its competence. The District Court in the decision in *New York Central Securities Corporation* v. *United States*, which this Court affirmed, in rejecting the contention that the rental dividends under a lease authorized by the Interstate Commerce Commission were inadequate, stated:

> "Adequacy of rental dividends depends upon a valuation of stockholders' equities in the light of normal returns upon similar properties. This matter, like that of valuation for rate-making purposes, is peculiarly within the competence of an expert tribunal." (54 F. (2d) 122, 128)

This Court in affirming the decree of the District Court stated as follows:

> "The remaining questions with respect to the adequacy of the rentals fixed, the other terms of the proposed leases, and the public interests involved, relate to the propriety of the action of the Commission in the exercise of its authority under the statute as construed. As to these matters the parties were fully heard, pertinent evidence was received and considered, and we find no basis for a contention that the order of the Commission was not adequately supported * * *." (287 U. S. 12, 29).

The "reasons" for the conclusion that the stock has no value were stated fully by the Commission in its report approving a plan of reorganization, in strict conformity

[1] The holding of the Court in that case is especially pertinent in the instant proceeding: "Here the controlling finding is not only that there was no equity in the property above the first mortgage but that petitioners' claims were appraised by the court as having 'no value'." (p. 27). The Court said: "Petitioners are the debtor, the holders of the second and third mortgages, and stockholders." (p. 26) See also decisions discussed on pp. 51-52 of this brief.

with the provisions of Section 77(e). (R. 2258-2260) The following reasons, among others, were stated by the Commission:

(1) "The last year when dividends were paid on the stock was in 1917." (R. 2259)

(2) "The record of the Milwaukee's earnings" from 1910 through 1938 supports the finding that the stock is without value. (R. 2259, referring to earlier statement in Commission's report on R. 2180)

(3) "Between 1930 and 1936 the income available for payment of interest, as adjusted by the committee and accepted by the debtor, varied between a high level of $20,298,074 and a low of $2,680,530, with an average of $10,270,360. Similarly adjusted, the available income in 1937 was $8,224,809 and in 1938 $6,023,296, bringing the average, 1930 to 1938, to $9,571,180. Future normal earnings were estimated by the committee at $15,894,000 a year. When these amounts are compared with the annual interest charges on the principal of the present debt, $23,739,000 a year, it is evident that the earning power of the system since the period of peak earnings is entirely inadequate to cover the principal of the debt, disregarding more than $118,000,000 of unpaid interest." (R. 2259)

(4) "We are required under section 77(e) to make findings in connection with the question of submitting the plan to the stockholders, and in doing so we must consider the aggregate amount of claims of the bondholders and other secured creditors in the light of the earning power of the system, past, present, and prospective, and all relevant facts. Unless an equity for the stockholders is established we are unable to find justification for their participation in the plan. *Case v. Los Angeles Lumber Products Co.*, ... U. S. ..... (Decided November 6, 1939)." (R. 2260)

The order of the District Court approving the plan provided:

"The Finding of the Commission that the equity of the preferred and common stockholders of the Debtor • • • has no value is affirmed." (R. 1991)

In thus affirming the finding that the stock is without value, the court considered not only the evidence certified by the Commission but also the voluminous oral and documentary evidence introduced in court. Some of the reasons stated by the court on the basis of this comprehensive evidence were:

(1) "The record shows that no dividends have been paid upon the stock of the debtor or its predecessor since 1917." (R. 1873)

(2) "Even in the ten-year period ending with 1930, which included the peak years of 1928 and 1929, income available for interest fell far short of the amount needed to service the funded debt which was less than on January 1, 1939, the effective date of the plan. This condition has been brought about not entirely by the financial depression but has been contributed to by many factors such as increased costs, taxes, wages, competition in other forms of transportation and the like. In no year since 1930 has the income available for interest been equal to the amount required under the proposed plan to meet charges ahead of dividends." (R. 1873)

(3) "The objectors [the debtor and the preferred stockholders committee] do not dispute any of the facts embodied in the elements considered by the Commission in reaching its conclusions but the contention is made that the outlook for the future is bright and the prospect for increased earnings promising and this situation, it is claimed, justifies a finding of some value for the equity owners. An expert was called who voiced this view and expressed at some length his opinion as to future earnings. That witness expressed the view that the debtor's properties were efficiently operated and were in good physical condition and that he felt, in the light of the present tendencies, that it was not too much to expect that a time might be reached sometime in the future, when the railroad might earn a sufficient amount to have available for the payment of interest $20,300,000. That time was referred to as the future normal year but the witness was unwilling even to venture a guess when such time might arrive.

Moreover, if such an amount were earned and available for the payment of interest, the capitalization of this amount at four per cent would produce slightly over $500,000,000 which is a less amount than the permissible capitalization fixed by the Commission. Under the plan approved by the Commission, if $20,300,000 were available for the payment of interest, there would only be enough to pay dividends on the new preferred stock and none on the new common, assuming the additional amount for additions and betterments contemplated by the plan were authorized by the board of directors, and the preferred stock under the plan represents the interest of present bondholders. If applied to the existing indebtedness, including unpaid accrued interest to January 1, 1939, such an amount would fall short by some $9,000,000 of paying interest at the average existing rate carried by the obligations of the debtor." (R. 1873-4)

On the record before it, the Circuit Court of Appeals passed on the finding that the equity has no value in precise and categorical terms, and sustained the action of the Commission and the District Court in respect thereto, stating in part:

"We are well satisfied that the evidence supports the finding of the Commission approved by the district court 'that the equity of the holders of the debtor's preferred stock and its common stock has no value.'

* * *

"If the Commission gave value to the common and preferred stock, it would have violated one of the first requirements of a valid reorganization as announced in the Consolidated Rock Products Company case. It would have taken property from the mortgagees and given it to the stockholders, an act which would not only have violated the law but would have transgressed all the rules of fairness which must be at the bottom of all reorganization plans." (R. 2311)

On motion by the preferred stockholders' committee to modify the opinion, the Circuit Court of Appeals further held on January 12, 1942:

"Now, to make our position entirely clear, we add

this memorandum and hold that the finding of the I. C. C. as to absence of value of old common and preferred stock, is specific, definite and certain, and fully meets the rule which requires finding on values of assets.

"Second, we meant to hold, and do hold, that the evidence supports this finding, that 'here is no value to either the common or preferred stock of debtor * * *.'" (R. 2335)

These conclusive reasons for the finding that the stock is without value, as stated by the Commission and both courts below, can not be controverted by the stock interests. They can not deny that since this property ceased to pay dividends in 1917 its earnings have failed to meet the interest requirements on its debt by an average annual amount of more than $6,000,000. Neither may they deny that the average normal prospective earnings estimated by the debtor's own witness in September, 1940, would fall short of meeting interest requirements by approximately $9,000,000 annually. (Opinion, District Court, R. 1873-1874) Faced with these past and prospective earnings, the debtor contended in its cross-petition that it prefers "to limit the discussion to the earnings of the Railroad Company for 1941 and the month of January, 1942." (Debtor's cross-petition for certiorari, p. 17) Substantially the same contention was presented to and rejected by the Circuit Court of Appeals. That court stated:

"This finding (that the stock is without value) is sharply challenged by the old stockholders who point to the present, sharp upturn of business activities, particularly railroads, stating that the first eight months of 1941 show an increase in gross operating revenues over 1940 of 22.8%, and estimate that the income available for fixed charges for 1941 will be $31,140,633. * * * We are well satisfied that the evidence supports the finding of the Commission approved by the District Court 'that the equity of the holders of the debtor's preferred stock and its common stock

has no value.' And this is true even though the evidence of current earnings made since the plan was approved, is received and considered." (R. 2310-2311)

Reliance by the stock interests upon wartime traffic and earnings disregards past experience. The temporary and illusory nature of such earnings is strikingly shown in the World War period 1914-1918 and its aftermath. While history never wholly repeats itself, a study of any war period shows quite conclusively that the entire economy of a nation is greatly distorted. We have available the effect upon this same railroad of the rise and fall in earnings co-incident with military activities and with a cessation of hostilities. The effect of the European war, which began in August, 1914, upon the traffic of American railroads was not measurably felt until 1916, when American exports rose from $2,716,000,000 in the preceding year to $4,272,000,000. (Sharfman, *The American Railroad Problem*, pp. 66-67) As a result of increased traffic due to war demand, railroad earnings in 1916 rose to an all-time high. In 1917, however, wage increases resulting from the Adamson Act of 1916, coupled with a rise in material prices, began seriously to cut into profits, even though gross revenues continued to rise. Finally, by proclamation of President Wilson dated December 26, 1917, the Government was compelled to take possession of the railroads in order to cope with increased material costs, insistent demands for further wage increases, car shortages, and congestion at the ports. (Sharfman, pp. 94, 119, 174) The railroads remained in Government operation until February 29, 1920. The experience of this railroad before, during and after the temporary bulge of war time earnings is shown in the following table, taken from Commissioner Lewis' opinion in the Commission's decision in the 1928 reorganization (131 I. C. C. 673, at 715):

Year[1]	Net Railway Operating Income
1912	$18,360,676
1913	27,580,419
1914	27,437,810
1915	25,198,955
1916	30,896,302
1917	21,657,112
1918	4,100,267
1919	1,969,322
1920 (deficit)	*14,497,698*

The Interstate Commerce Commission has characterized wartime traffic and earnings thus: "We know from past experience that the upswing in business which war brings is temporary and likely to be followed by an aftermath in which conditions will be worse than before." (Fifty-third Annual Report of Interstate Commerce Commission to Congress, p. 5)

In hard fact, the Commission faced a situation presented by the dismal failure of a plan of reorganization which had been evolved in an equity reorganization of this same railroad only a few years before. As we have pointed out, the criticisms of that plan current at the time of its approval and consummation are to be found in the Commission's reports.[2]

The 1928 plan increased total capitalization, increased debt and total interest charges (part of which were made

[1] Years 1913 to 1915, inclusive, were fiscal years ending June 30 of each year; the others are calendar years. The railroad was operated by the Federal Government in 1918, 1919 and the first two months of 1920.

[2] *Investigation of Chicago, Milwaukee & St. Paul Railway Company*, 131 I. C. C. 615 (1928), and *Chicago, Milwaukee & St. Paul Reorganization*, 131 I. C. C. 673 (1928). The first of these reports dealt with the causes leading to the failure of debtor's predecessor in 1925, and the second with the approval of securities under the 1928 plan of reorganization. Likewise, criticisms of the plan and the activities of reorganization managers thereunder are to be found in the dissenting opinion of Mr. Justice Stone in *United States* v. *Chicago, Milwaukee, St. Paul & Pacific R. R.*, 282 U. S. 311, 331-44 (1931).

contingent upon earnings) and retained the former stockholders as equity owners of the reorganized company. (131 I. C. C. 673) Although no dividends had been paid on either the common or preferred subsequent to 1917,[1] the old stockholders kept their former position in the capital structure. The only burden placed upon them was the payment of an assessment of $28 and $32, respectively, per share of preferred and common stock, for which they received new bonds (Fifty Year Five Percent. bonds) at par for all but $4 of each assessment, this $4 being reserved for reorganization expenses or working capital in the discretion of the reorganization managers.[2]

From the approval of the securities in the 1928 reorganization, four of the eleven commissioners dissented and the majority recognized "shortcomings" in the plan which were passed by "solely upon the ground that the major public interest seemed to us to require that the properties should at the earliest possible moment be released from receivership and restored to active management by those financially interested therein." (131 I. C. C. at 699) The dissenting commissioners were especially critical of the failure to reduce capitalization and interest charges and the retention of the old stockholders. Thus Commissioner

[1] As to the source of the payments to stockholders in the years prior to suspension of all dividends in 1917, the Commission, in its *Chicago, Milwaukee & St. Paul Investigation*, said: "'All dividends paid prior to July 7, 1910, were paid out of income. The semi-annual dividend declared on that date was paid out of surplus, the next dividend was paid out of income, and all subsequent dividends were paid out of surplus. The last dividend paid was declared on July 26, 1917." (131 I. C. C. 615 at 626)

[2] It was this $4 per share which the Commission, in its order approving the security issues, required to be impounded as a separate fund "not to be paid out unless and until so authorized by order of the court in respect to payments subject to the court's jurisdiction or by this commission." (131 I. C. C. 673 at 725) It was the validity of this provision which the reorganization managers successfully attacked in *United States* v. *Chicago, Milwaukee, St. Paul & Pacific R. R.*, 282 U. S. 311 (1931).

Eastman, with whom Commissioners McManamy and Campbell joined, said:

> "The conclusion from these facts is inescapable that the sacrifice under the proposed reorganization plan is a sacrifice on the part of the holders of the defaulted bonds and that the stockholders, who were apparently wiped out by the foreclosure sale, are being restored to their original position with very little sacrifice." (131 I. C. C. at 709)

Commissioner Lewis, who likewise dissented, said:

> "Anyone who reads the report covering the investigation made into the causes of the St. Paul receivership, which is issued concurrently with this authorization of reorganization, must wonder just how these old stockholders get into the new company on the terms offered. It must be recalled that they lost their property by neglect, that is, failure to manage it." (131 I. C. C. at 718)

In the present reorganization proceedings the Commission found that these old stockholders, or their successors in interest, had no rights which could survive this second financial failure in a single decade. These findings have been held adequate, lawful and inescapable by both of the courts below.

(c) Findings as to the Additions and Betterments Fund.

The Commission's plan provides that there shall be created an additions and betterments fund for purposes which are specified in detail, into which shall be made certain annual payments. The fundamental and single purpose of the additions and betterments fund which the Commission has prescribed is to enable the property to exist as a going concern capable of performing its public function. Under the Commission's accounting regulations,[1] the day to day routine maintenance of the property in-

[1] Accounting Classifications Prescribed by the Interstate Commerce Commission (revised to January 1, 1941), especially pages 13, 17, and 19-44.

volves charges to additions and betterments. When a bridge must be replaced because it has been worn out and become unsafe, the additional cost of the new bridge over the original cost of the old bridge is charged to additions and betterments notwithstanding the fact that it may be of exactly the same type and capacity, and perform precisely the same function as the old bridge. As rail wears out it is almost invariably replaced with heavier rail. Considerations of safety, greater speed, the effect of heavier motive power, and other changes in the art, made the use of the heavier rail not a matter of choice but of necessity. Nevertheless, its use involves, in an accounting sense, a betterment, and the cost of the excess weight is charged not as an operating expense, as it is fundamentally, but to capital account. What is true of bridges and rail is true of every other depreciable element of the property. Each year the railroads are required by public authority, in the public interest, to spend large sums for grade separations, for crossing protection, for safety appliances sought by the employees, or for other projects and facilities deemed necessary by some regulatory authority. Expenditures for these purposes are classified as additions and betterments, but in the main, for the reasons stated, they do not produce additional income. Primarily they are necessary either to prevent the deterioration of the property and so to sustain its earning power, or to satisfy requirements which are incident to the performance of its public function.

The revenue which must be devoted to such expenditures, which are as much an incident of the normal and proper operation of the road as the payment of wages, is not in any true sense income. The real income is that, and only that, which remains after these unavoidable operating costs have been paid. Hence the Commission found that the plan must provide for the creation of an adequate additions and betterments fund with a call on income before payment of contingent interest charges.

The treatment of this provision of the plan by the Circuit Court of Appeals is illustrative of its opinion, and, we believe, forcefully demonstrates the error in its conception of *Palmer* v. *Massachusetts* and the *Consolidated Rock Products* case. The entire discussion of the additions and betterments fund by the Circuit Court of Appeals was as follows:

> "The serious attack made on that portion of the plan which calls for the mandatory payment of $2,500,000 into the additions and betterments fund, calls for no extended discussion. Counsel contend that the sum is excessive and unfair and does not affect all security holders equally. We think otherwise.
>
> "While there must be more fact findings upon which to reach a final conclusion on this, as well as the other phases of the plan, we believe the Commission is entirely sound in its position that a fund for additions and betterments should be created. In fact we find few things in the plan which appeal stronger than this provision.
>
> "Failure to provide against financial and commercial storms and other adversities which affect railroads, like other industries, accounts fo. much of the condition of the railroads today. The possible avoidance of such recurrence will be aided by this or a similar provision. It would be improper to pass directly upon the reasonableness of the amount, however, until the findings which must be made are before us. However, we may say that there is evidence that would amply warrant an allowance for such an item, and also the amount adopted by the Commission. But findings there must be, based on the evidence, which support both the allowance and the amount of the allowance." (R. 2313)

In most specific terms the Commission found that there should be an additions and betterments fund and found the amount necessary for the fund. The Circuit Court of Appeals determined that the sum was not excessive or unfair. Nevertheless, the court felt itself constrained to reverse the District Court's approval of the plan and to remand the proceedings back to the Commission

for further findings of fact. We submit that such a view of the administrative process, conceived and provided by the Congress to effectuate the reorganization of the railroads, is erroneous and would strike a severe blow to the entire administrative machinery of the government.

The findings and conclusions of the Commission as to the additions and betterments fund are more than adequate, as a brief survey will show.

The Commission first summarized the terms proposed by the parties for the fund, and the debtor's showing of the annual charges to additions and betterments each year from 1928 to 1937, together with a statement of the cash obtained each year from equipment depreciation charges, road retirements, and salvage, and the testimony as to future needs of the property. (R. 2192, 2203) On the basis of the full consideration of the subject the Commission stated:

> "It appears that the committee considers that approximately $10,700,000 of cash will be available annually for the additions and betterments fund and the reserve and retirement fund, such amount including retirements, salvage, and depreciation on equipment, while the debtor estimates its average capital requirements for the next five years at about $12,900,000 a year, leaving $2,200,000 or more, which, if the expenditures were not curtailed, would have to be financed by the issue and sale of new securities. Testimony for the debtor tends to support the foregoing estimate of future requirements but in such a matter exactness cannot be expected. We think that the situation will be met by the provisions for the additions and betterments fund hereinafter made, by which the contributions to the fund in respect of any income period will be part mandatory and part in the discretion of the management." (R. 2223)

Thereafter the Commission stated in specific detail the terms of the additions and betterments fund approved by it. (R. 2237-2241)

In its supplemental report the Commission again reviewed the evidence of the needs of the property, and made a change in the provision for the payments into the fund. (R. 1287-1292, 1293-1294) We direct particular attention to the Commission's lengthy statement of its findings and conclusions on this subject on page 1289 of the record.

These many findings, based upon a careful consideration of the evidence and the reasons for an additions and betterments fund and the terms thereof, were not referred to by the Circuit Court of Appeals. We submit that the report of the Commission meets the requirements of the statute that "the Commission shall state fully the reasons for its conclusions" and that the holding of the court that the Commission should include in its report "more fact findings upon which to reach a final conclusion on this" (R. 2313) would serve no useful purpose and would frustrate the practical operation of the statute.

(d) Findings as to Each of the Several Mortgage Divisions.

Inasmuch as the fixed and contingent interest permissible under the Commission's plan was inadequate to service all of the claims of secured creditors of the bankrupt company, it became necessary for the Commission to determine a fair and equitable method of apportioning the bonds and stocks of the reorganized company to the various classes of creditors of the old company. In so doing, the Commission investigated with care and made numerous findings as to the relative earning power of the different divisions, their relative importance to the reorganized company, the desirability of their continued operation in the public interest, and their value in terms of new securities of the reorganized company.

1. GENERAL MORTGAGE.

One of the controversies before the Commission related to the claims of the holders of the General Mortgage bonds, as contrasted with the claims of the holders of the Fifty Year Five Per Cent. Mortgage bonds and the holders of the bonds of the Chicago, Terre Haute and Southeastern and its subsidiaries. The Commission's report states findings on which it based its conclusions as to the relative amount and nature of the securities of the reorganized company which each of these claimants should receive.

Thus, the several series of General Mortgage bonds, their amounts, interest rates and maturity date were described by the Commission at R. 2166-2167. The Commission described the property subject to the first lien of this mortgage, including miles of road and number of locomotives, freight cars, passenger cars and work equipment. (R. 2167) It found that there were no equipment deficiencies under this mortgage. (R. 2167)

The Commission fully reviewed the history of the road, its traffic sources and density, and earnings. It also found that the original cost of this division was $392,703,461, cost of reproduction new $472,238,990, cost of reproduction less depreciation $290,636,520, and value of lands and rights $68,479,079. (R. 2215, 2250; I. C. C. Bureau of Valuation Report, Sheet 4)

An earning study was made for the year 1936 (the latest year for which the necessary statistics were then available) in which net earnings were the best the property had experienced since 1930. (R. 2180) The Commission found that in 1936 the earnings of the general mortgage lines were $8,716,847, or $7,561,688 after deducting charges on equipment obligations. (R. 2250) The Commission stated:

> "The latter sum is 1.16 times interest charges on the general mortgage bonds, including the series G bonds pledged with the Finance Corporation." (R. 2250)

"Thus on the basis of income available in 1936 for payment of interest, stated above, the Northern's consolidated mortgage bonds are on a parity with the general mortgage bonds. * * *

"We conclude that the holders of the debtor's general mortgage bonds and the holders of the Northern's consolidated mortgage bonds should be accorded similar treatment under the plan * * *." (R. 2251)

In view of the earnings of the property in the light traffic years which had just been experienced, and like periods reasonably to be anticipated in the future,[1] and under the necessity of establishing a substantial charge against income for the additions and betterments fund, the Commission found that it could not safely commit the reorganized company to the payment of an annual fixed charge for the entire system of more than $4,269,654 (R. 1298, 2219) which is equal to about one-third the income for the year 1936 covered by the studies.

In connection with its findings as to the General Mortgage bonds, the Commission also found, after making provision for the claims of the Reconstruction Finance Corporation and for the holders of the Milwaukee and Northern First Mortgage bonds, as follows:

"The new bonds remaining available under our plan, after provision for the claims just mentioned and for new money, will consist of approximately $40,421,864 of first mortgage bonds and $108,012,719 of general mortgage bonds, series A and series B, while the secured creditors for which provision remains to be made consist of five classes holding, respectively, $5,072,000 of Northern consolidated mortgage bonds,

[1] "A plan of reorganization within the meaning of this section * * * (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; * * *." (Section 77(b))

$138,788,000 of the old Milwaukee's general mortgage bonds, $106,395,096 of the debtor's 50-year mortgage bonds, $182,873,693 of the debtor's adjustment mortgage bonds, and $3,000,000 of the Gary first mortgage bonds. Including unpaid interest accrued to December 31, 1938, these claims amount to approximately $555,000,000." (R. 2250)

The Commission then made its further findings regarding the General Mortgage bonds, declaring:

"Because of their first lien position and the earnings available for interest, the general mortgage bonds and the Northern consolidated mortgage bonds take precedence over the other claims just mentioned above. The general mortgage liens are those upon which the other divisions are largely dependent for revenue." (R. 2250)

Within the limits of the permissible total capitalization and total fixed charges and the allocations required for all other classes of creditors, the Commission concluded that the holders of the General Mortgage bonds and the Milwaukee & Northern Consolidated bonds should receive securities of the new company on the basis of new first mortgage bonds equal to 25 per cent of their total claim, including unpaid interest, new general mortgage bonds, series A, equal to 35 per cent, new general mortgage bonds, series B, equal to 20 per cent, and new preferred stock of par value equal to 20 per cent. (R. 2251)

The District Court considered objections to the treatment of General Mortgage bonds in the Commission's plan as made by the trustee under the General Mortgage and by a small group of General Mortgage bondholders. (R. 1886-1889) After stating that the basis of distribution of new securities is "not capable of exact mathematical computation," the District Court said:

"The Commission and the Court are required to make and approve a fair and equitable distribution of the securities available and the Court believes that this has been done in this instance." (R. 1889)

The Circuit Court of Appeals considered the objections

of certain general mortgage bondholders to the plan and concluded:

> "Accepting, as we do, the necessity for a drastic reduction in indebtedness and interest requirements and realizing that each of these divisions, to a certain extent, depends upon the existence and business of other branches of the system, *we are unable to say the evidence fails to establish the fairness of the plan so far as these bonds are concerned.*
>
> "If the proposition were an original one, it is true, we can readily see how a larger percentage of the new plan first mortgage bonds might have been given to holders of the General Mortgage bonds. On the other hand, while there is a difference in the priorities of the first mortgage bonds and the Series A bonds of the new issue, this may be made up in increased interest rates of the new bonds, especially if the increased revenues of the company, as disclosed during the year 1941, are maintained even in part. There is, however, in our opinion, a serious question presented due to the small percentage (25%) of the First Mortgage bonds given to the holders of old General Mortgage bonds. Our suggestion is that if any revision should be made, this percentage might be increased and the percentage of Series B and preferred and common stock, reduced."[1] (R. 2312-2313)

---

[1] This statement illustrates, we believe, the vast difference which exists between a consideration of specific objections to various provisions of a plan, treating each, as did the Circuit Court of Appeals, as a more or less independent and isolated subject, and the responsibility borne by the Commission of formulating a complete plan dealing with the relative rights and interests of all parties.

It is entirely clear from the court's opinion as a whole, that it did not mean to imply that this road, twice bankrupt within seven years, should issue more of the first mortgage bonds, and thus be burdened with a higher annual fixed charge than that established by the Commission. To follow the court's suggestion would require, therefore, that some other class of creditors which participate in the first mortgage bonds under the provisions of the plan, must suffer a corresponding reduction in their allotment. The court does not suggest what other allotment of the new first mortgage bonds might be reduced. It is evident that the court gave no consideration to that aspect of the problem. The findings of the Commission, supported by the record, show that

The court thus concluded that the evidence supported the fairness of the treatment of the Generals. There is no other reference in the opinion to the treatment of the General Mortgage bonds unless the court's general comment at the end of the opinion as to the necessity for additional findings may also refer to this issue.

2. FIRST AND REFUNDING MORTGAGE.

All of the bonds issued under the First and Refunding Mortgage aggregating $9,866,000, except $943,000 held in the debtor's treasury (R. 2170), were pledged, along with other securities, as collateral security for loans from the Reconstruction Finance Corporation and for a Public Works Administration loan subsequently acquired by the Reconstruction Finance Corporation. (R. 2173) The series M equipment trust certificates also were subsequently acquired by the Reconstruction Finance Corporation from the Public Works Administration. (R. 2173) In addition to being a first lien on a large trackage, lying mostly west of the Missouri River, the mortgage was further secured by a

---

the rights of the other creditors participating in the distribution of fixed interest securities are either equal or superior to those of the Generals. These are the holders of equipment trust certificates on the equipment necessary to operate the system, the Reconstruction Finance Corporation (a collateral noteholder whose treatment in the plan is not attacked by anyone) and the Milwaukee & Northern mortgages (one of which earns at approximately the same rate as the General Mortgage lines, and the other at a much higher rate). It was only after the fullest consideration of these claims independently and in relation to one another that the Commission made its allocation to each, stating fully the reasons for its conclusions as required by Section 77. The relationship between the Generals and the Fifty Year Five Per Cent. Mortgage bonds is of no importance in this connection because those bonds do not participate in the first mortgage bonds.

A modification requested by the General Mortgage trustee which would increase the fixed interest bonds allotted to the Generals was refused by the Commission, which found that "within the limits of total capitalization and total fixed charges approved, any material changes in the distribution of the new securities would render the distribution less equitable from the standpoint of relative rights." (R. 1304, 1307)

pledge of the leasehold interest under the Terre Haute lease, some equipment, a large amount of stocks and bonds of other railroad and terminal companies and by $789,133 in cash held by the trustee of the mortgage on January 31, 1938. (R. 2171) The mortgage was further secured by a second lien on properties as to which the General Mortgage, the Milwaukee & Northern first mortgage, the Gary mortgage and the Bellingham Bay & British Columbia mortgage had first liens and by a third lien on properties under the second lien of the Milwaukee & Northern consolidated mortgage. (R. 2171)

The Commission found that the First and Refunding Mortgage Bonds pledged with the Reconstruction Finance Corporation represented a first lien on physical property, securities and cash, the value of which without question exceeded the amount due the Reconstruction Finance Corporation. (R. 2246) In this connection it referred to testimony as to the scrap value of the rail alone on the western lines subject to the first lien of the mortgage, the report of the Commission's Bureau of Valuation on the elements of physical value of the lines; and the assets, earnings and dividend record of terminal companies whose stock was pledged under the mortgage. (R. 2247) It concluded that, inasmuch as all outstanding bonds under this mortgage were held by the Reconstruction Finance Corporation and the mortgage would be cancelled under the plan, the Reconstruction Finance Corporation should receive all the cash in the possession of the First and Refunding Mortgage trustee at the time of consummation of the plan. (R. 2247) For the remainder of its debt, Reconstruction Finance Corporation receives, under the plan, new first mortgage fixed interest four per cent bonds. (R. 1317)

The Circuit Court of Appeals stated, with reference to the First and Refunding Mortgage bonds which constitute part of the Reconstruction Finance Corporation collateral:

"No challenge of the plan is made so far as it affects this mortgage." (R. 2304)

Reconstruction Finance Corporation, while contending for more favorable treatment as a creditor in the proceedings before the Commission, accepted the plan certified by the Commission and in the proceedings before the District Court sought its approval. (R. 1867) It also appeared in the Circuit Court of Appeals seeking affirmance of the order of approval of the District Court and through action of the Solicitor General was a petitioner for a writ of certiorari to this Court to review the decision of the Circuit Court of Appeals, which was granted by this Court on June 8, 1942. (No. 32)

3. FIFTY YEAR FIVE PER CENT. MORTGAGE.

The Commission's consideration of the claims of the holders of bonds issued under the Fifty Year Five Per Cent. Mortgage was extensive because of the aggressive insistence of such holders throughout the proceedings that their security entitled them to more favorable treatment than that accorded them in any plan submitted to the Commission.

The Commission found that there were $106,395,096 of bonds issued under this mortgage, that the interest requirements were $5,319,755 yearly, and that as of December 31, 1938, there was accrued unpaid interest of $20,835,706. (R. 2172). The original cost of the property subject to the prior lien of the Fifty Year Five Per Cent. Mortgage, after payment of the claim of the Reconstruction Finance Corporation, was found to be $217,052,949, the cost of reproduction new $252,468,812, the cost of reproduction less depreciation $190,054,042, and the value of lands and rights $7,929,980. (R. 2247; I. C. C. Bureau of Valuation Report on Elements of Value, Sheet 3)

The Commission dealt at length with the most extensive

and complicated earnings studies covering the lines subject to this mortgage (R. 2252) and considered in detail the issues which had been raised as to the computation of such estimates of earnings and their use with respect to the treatment of these bonds. On the basis of this exhaustive consideration of the matter, the Commission held that the treatment proposed by its Examiner "would result in their participation with senior creditors when the system income available for interest exceeds $6,364,602, after payment of $2,500,000 to the additions and betterments fund We do not consider such treatment of the 50-year bonds to be justified on any basis of earnings shown." (R. 2254).

The Commission stated that under the treatment allotted the Fifty Year Five Per Cent. bonds in the approved plan,

> "* * * they will begin to share earnings with the general mortgage bonds and Northern consolidated bonds after $9,675,000 of prior charges * * *. We think that this treatment goes far toward resolving the doubts as to the accuracy or fairness of the allocation of earnings in favor of the 50-year bonds, without injustice to the general mortgage bonds. * * * We see no means by which the exact present lien position of the general mortgage bonds or the 50-year bonds can be preserved except under a prohibitive mortgage structure.
>
> "We conclude that the holders of the 50-year bonds should be entitled to receive the securities of the new company as provided herein, * * *." (R. 2254-2255)

In its supplemental report the Commission again considered the earnings estimates and the earning power of the western lines. (R. 1305, 1307-1308) It also said:

> "The elements of physical value referred to were before us, and were considered by us. * * * It is clear that in the light of the above described evidence as to earning power of the western lines, the same weight cannot be accorded the physical value of the properties as might be under conditions of higher earning power." (R. 1308)

The District Court considered the objections to the Com-

mission's plan of the mortgage trustees and the protective committee for holders of Fifty Year Five Per Cent. mortgage bonds. (R. 1889) It stated its conclusions in respect thereto as follows:

> "The fact is, however, that under the situation presented to the Commission and to the Court, the Fifty Year bonds are in the position of second lien bonds with a poor earnings record. Some complaint was voiced as to the method followed in arriving at the allocation of earnings used in the exhibits but no better method was suggested and no sound reason was advanced in support of a different result." (R. 1889)

The Circuit Court of Appeals discussed briefly the objections of these same objectors on appeal and concluded:

> "Accepting the rule there announced [in the *Consolidated Rock Products* case] for determination of value (to-wit, earning power) the *5's of '75 have, we think, no legitimate complaint.* Sec. 77 (e) does not change our conclusion." (R. 2312)

There was no further comment as to these bonds in the opinion, unless the general comment upon the need for more findings may be taken as referring also to that issue. It is not clear whether the Circuit Court of Appeals intended to criticize the Commission's findings thereon. If it did so intend, the holding, we believe, is unsound in the light of the extensive findings by the Commission on the position of this mortgage in the debtor's capital structure.

4. CONVERTIBLE ADJUSTMENT MORTGAGE.

These bonds have been issued in the principal amount of $182,873,693, carry a 5% interest rate, and mature January 1, 2000. The accrued and unpaid interest amounted to $79,550,055 as of December 31, 1938. (R. 2172) They are secured by a lien on the same property as the Fifty year Five Per Cent. bonds but immediately junior to that mortgage. (R. 2172)

Since these bonds are a lien on virtually the entire sys-

tem but subordinate to other mortgages, the question as to them was largely whether the total permissible capitalization of the property was such that the satisfaction of the claims of senior creditors left anything for distribution to these bondholders.

The Commission's conclusions as to the Convertible Adjustment bonds were, in part, as follows:

> "As compared with the above-stated charges on the debt ahead of the adjustment mortgage bonds, the system income available for interest, as adjusted by the committee, averaged $21,038,461 a year during nine predepression years 1921-29. During the succeeding nine years, 1930-38, the average was $9,571,180, and during the entire 18 years it was $15,304,822. In the discussion of stockholders' equity which follows we take the position that the peak earnings of one or two years in the past cannot be relied on as indicative of an earning power sufficient for a finding that the equity is of value. In the case of the adjustment mortgage bonds the situation is different in that the charges on all prior-lien debt were more than covered over a long period of time prior to the depression and are nearly equalled by the average earnings during the past 18 years, as well as by the earnings predicted for the future normal year. As compared with a debt of approximately $364,000,000 ahead of the adjustment mortgage bonds, the cost of reproduction of the system properties, less depreciation, plus the value of lands and rights, an allowance for working capital, and the net additions and betterments reported by the carriers in 1936 and 1937, was $662,759,838. We consider that the issue of new common stock to the adjustment mortgage bondholders, as proposed by the committee, is justified, but not in the amount proposed. The plan we approve advances the position of the adjustment mortgage bonds over that of the committee's plan since the charges ahead of the new common stock will be reduced by some $1,635,000 below those shown in the committee's plan, on the basis of a $2,500,000 additions and betterments fund in each case." (R. 2256)

The Commission found that the above allotment of stock "will fail to satisfy the claim by $55,471,653. For this portion of their claim, these bondholders should be permitted to participate with other unsecured creditors in the free assets of the debtor." (R. 2257) It also found: "This additional assignment, in respect of the debtor's free assets, is on the basis of approximately 0.7 share to each $1,000 of claim, and the same basis should be followed in the treatment of all other unsecured claims allowed by the court." (R. 2257)

The Commission analyzed the free assets, which consisted chiefly of the stock and notes of the Milwaukee Land Company and found:

> "Considering the above indications of value we find that not exceeding 55,000 shares of new no-par-value common stock may be issued against the debtor's unpledged interest in the land company approximately on the basis of capitalization followed in establishing the new capital structure for the properties subject to mortgages." (R. 2260-2261)

The District Court stated:

> "The Commission allotted to them [the Adjustment bondholders] out of the permissible capital structure all that was left after satisfying prior claims. It could do no more." (R. 1891)

The Circuit Court of Appeals made no analysis of the Commission's report on the allocation to the Convertible Adjustment Mortgage other than to state that more findings were necessary. (R. 2314)

5. MILWAUKEE & NORTHERN MORTGAGES.

Milwaukee & Northern First Mortgage bonds are outstanding in the principal amount of $2,117,000 and Milwaukee & Northern Consolidated Mortgage bonds are outstanding in the principal amount of $5,072,000. No appeal was taken by anyone interested in these bonds from the order of the District Court sustaining the plan.

The Commission found:

> "The Northern first mortgage is secured by a lien on approximately 110 miles of wholly owned line and 16 miles of jointly owned line, lying between North Milwaukee and Green Bay, Wis., together with certain old cars. The consolidated mortgage is secured by a first lien on approximately 268 miles of line situated north of Green Bay, and by a second lien on the line south of that point." (R. 2168)

The property subject to the lien of the Northern First Mortgage had an original cost of $4,235,832, cost of reproduction new, $5,163,026, cost of reproduction less depreciation, $3,533,265 and the value of its lands and rights is stated at $751,021. (R. 2248; I. C. C. Bur. of Valuation Report on Elements of Value, Sheet 1)

The property subject to the first lien of the Northern Consolidated Mortgage had an original cost of $9,025,562, cost of reproduction new, $10,855,672, cost of reproduction less depreciation, $7,932,507, and the value of its lands and rights is stated at $290,624. (R. 2251; I. C. C. Bur. of Valuation Report on Elements of Value, Sheet 2)

The Commission found that the analysis of the Northern's earnings for the 12 months ended September 30, 1933, and for the year 1934, showed earnings available for interest of $228,236 and $370,016, respectively, in those periods, as against total interest charges of $323,505 per annum. (R. 2248) The estimate of 1936 earnings, which the Commission found was prepared partly on the basis of treating the Northern as a separate road and partly as a unit of the system, showed for the test year 1936, for the Northern lines as a whole, $495,182 income available for interest. (R. 2248, 2249) It also showed the 1936 net earnings of other system lines from traffic interchanged with the Northern, namely, $524,915. (R. 2248) The separation of the 1936 earnings of the Northern showed $411,633 income available from the First Mortgage line,

as against interest of $95,265, and $83,549 as income available from the Consolidated Mortgage first lien line, as against $228,240 interest on the Consolidated bonds. (R. 2248-2249) If the 1936 computations were placed on a strictly system basis, the earnings on the First Mortgage line would be reduced approximately $125,000. (R. 2249) The interest on those bonds was earned three times over in 1936 even on the lower basis. (R. 2249) The Commission further found that the interest on the Consolidated bonds was earned about 1.2 times in 1936 when the excess of the First Mortgage earnings over interest is credited to the Consolidated Mortgage. (R. 2249)

It stated that "From the evidence regarding the elements of value and earning power of the Northern first mortgage lines we conclude that" the Northern first mortgage bondholders are entitled to receive 70% of their claim in new first mortgage 4% bonds and 30% in new general mortgage 4½% bonds, Series A. (R. 2249)

Having regard at all times for the fact that it was dealing with relative rights the Commission further found that

> "* * * on the basis of income available in 1936 for payment of interest, stated above, the Northern's consolidated mortgage bonds are on a parity with the general mortgage bonds." (R. 2251)

Accordingly, it allotted identical treatment to the General Mortgage bonds and to the Northern Consolidated bonds. (R. 2251)

The District Court considered extensively the position of these bonds and the treatment accorded them. (R. 1885-1886) It concluded:

> "It appears that in the light of the facts disclosed by the record and with the limited capitalization and fixed interest charges necessarily imposed by the plan, the treatment received by these securities was all that they could reasonably expect and was, under the circumstances, fair and equitable." (R. 1886)

The Circuit Court of Appeals did not discuss these bond issues, but mentioned them in a general statement that more specific findings were necessary. (R. 2314)

6. THE TERRE HAUTE LEASE.

The debtor is lessee of a line of railroad owned by the Chicago, Terre Haute & Southeastern Ry. Co. The Terre Haute lease, which is for 999 years, was executed in 1921 to the debtor's predecessor. By the terms of the lease the debtor is liable both for interest ($1,023,580) and principal ($21,929,000) on the four issues of Terre Haute bonds, together with an amount up to $12,000 yearly to pay Terre Haute corporate expenses, and is obligated to maintain Terre Haute equipment. (R. 2169) The liabilities of the debtor for vacancies in performing this latter obligation were estimated at $5,000,000 as of June 30, 1935, $6,832,556 as of December 31, 1936, and $7,106,149 as of December 31, 1937. (R. 2170)

The Commission found the provisions of the existing lease to be so burdensome that an adoption of the lease by the reorganized company would "jeopardize a successful reorganization of the Milwaukee" and that its rejection "is a necessary step in order that the processes of reorganization of the Milwaukee may not be thwarted." (R. 1303) The Commission said:

> "We have been and remain strongly of the opinion that the plan should pr ide some means for retaining the Terre Haute lines as a part of the system without unduly jeopardizing a successful reorganization of the Milwaukee." (R. 1303)

Congress did not leave the Commission powerless to deal with the situation presented by the Terre Haute lease. Although the Commission concluded that technically it lacked power to force a consolidation of the Terre Haute with the Milwaukee (R. 2213-4), Congress conferred the neces-

sary power on the Commission to deal with the situation by providing in Section 77(b) that:

> "A plan of reorganization * * * may reject contracts of the debtor which are executory, in whole or in part, *including unexpired leases; and may include any other appropriate provisions not inconsistent with this section.*"

After considering all elements of value of the Terre Haute and the relative contributions of the Milwaukee and the Terre Haute to the joint enterprise, the Commission dealt with the Terre Haute lease in a manner that conforms strictly to this basic statutory authority.

The mileages subject to the liens of the respective Terre Haute mortgages were described by the Commission. (R. 2169-2170) The Commission found that the original cost of the Terre Haute property was $24,086,120, the cost of reproduction, $27,994,556, the cost of reproduction less depreciation, $19,357,027, and the value of lands and rights $1,323,087, in comparison with the outstanding Terre Haute bonds which aggregate $21,929,000. (R. 2164, 2169, 2212)[1]

The Commission stated the estimated earnings of the Terre Haute for 1936 on both the tariff rate basis for haul of company coal and other material, and on the cost of service basis. The respective amounts were $2,990,126 and $2,040,187. (R. 2212) Similar amounts were stated for the years 1925, 1926, 1933 and 1934. (R. 2213) But these so-called earnings of the Terre Haute property are largely

[1] The facts concerning the acquisition in 1921 of the Chicago, Terre Haute & Southeastern and its subsidiaries by debtor's predecessor, Chicago, Milwaukee & St. Paul Railway Company, were thoroughly investigated by the Commission. *Chicago, Milwaukee & St. Paul Investigation*, 131 I. C. C. 615 at 653-660 (1928). It found that the Terre Haute "was a distress property controlled by a committee of Chicago bankers who wanted to liquidate and who had written the securities off the books of their banks as 'losses'" (pp. 657-658); that "the terms upon which the property was acquired were improvident and to that extent adversely affected the financial condition of the St. Paul" (p. 657).

dependent upon its position as a part of the Milwaukee system, and upon the power of the system to obtain, to hold, and to control the routing of traffic. The Commission found:

> "It may be safely concluded that the earning power of the Terre Haute is sufficient to cover all interest requirements, but this earning power is largely dependent on a continuation of the Milwaukee's coal traffic, together with the commercial coal traffic that accompanies it, and would be greatly diminished if such traffic ceased. The present arrangement is distinctly to the advantage of the Terre Haute." (R. 2213)[1]

The Commission discussed at length whether it had jurisdiction to deal with the Terre Haute lease by consolidating that road with the debtor and concluded it lacked that power. It then carefully considered and stated the necessity for reduction of fixed charges, and compared the security of the Terre Haute bondholders with that of other bondholders. (R. 2214-2216) Having found that the earnings of the Terre Haute were dependent upon system traffic, the Commission concluded that if the lease were to be adopted the Terre Haute must also share in the burdens of the system, and receive treatment fairly and equitably related to that accorded other creditors. The Commission's statement is as follows:

> "Under the circumstances, we shall approve as part of the plan, provisions for dealing with the Terre Haute bonds *in a manner which bears a fair and equitable relationship to the treatment accorded the bondholders of the debtor*, does not require a consolidation of the properties, and yet accords to the Terre Haute bondholders the same security under the existing mortgage, respectively, as their present bonds hold. However, these provisions, in order to become an effective part of the plan, will have to be accepted by substantially all of the Terre Haute bondholders." (R. 2216)

The Commission provided that an offer be made to the

[1] See also R. 1513-23, 1621, 1694-9.

Terre Haute bondholders for their voluntary acceptance or rejection. The principal terms of the offer are that the reorganized company will lease the Terre Haute line only if the interest rate on the Terre Haute bonds is modified, the maturities are extended, and the equipment vacancies are waived.[1] If the offer is not accepted, the lease is to be rejected. (R. 2216-2218)

In its supplemental report, the Commission refused to increase the amount of fixed interest for Terre Haute bonds to be provided in the offer, and found that "no increase in the amount of future fixed charges should be permitted." (R. 1298)

Also in the supplemental report, the Commission considered fully, and rejected, the proposal of the Terre Haute bondholders that the existing lease be assumed by the new company. After referring to the legal obstacle to consolidation, the Commission stated its conclusion, in part, as follows:

> "Despite this fact the Terre Haute is in practical effect a part of the Milwaukee system, its bondholders are essentially system creditors, and a disruption of the lines would be to the disadvantage of both companies. We have been and remain strongly of the opinion that the plan should provide some means for retaining the Terre Haute lines as a part of the system without unduly jeopardizing a successful reorganization of the Milwaukee. In harmony with this idea we inserted in the plan the provisions outlined above, which were the best that we could devise in the public interest and as affording fair and equitable treatment to both the bondholders of the Terre Haute and those of the debtor." (R. 1303)
>
> "In the event of rejection there would seem to be no alternative but a rejection of the present lease, and the plan so provides. Such rejection is not intended as

[1] The Terre Haute bondholders would retain their bonds as modified (R. 2316, 1301), and not (as the court below stated) (R. 2305, 2314) receive bonds of the new company.

a threat. It is a necessary step in order that the processes of reorganization of the Milwaukee may not be thwarted. Without rejection of the lease the difficulties of effecting a reorganization, along the lines of the capital structure shown in the approved plan, are evident. • • • Under these circumstances we consider that there is no justification for the approval of a plan based upon the assumption by the new company of the lease, the guaranty of the Terre Haute income bonds, and the other obligations growing out of the lease." (R. 1303-1304)

The Commission, therefore, after having considered the terms of the lease, the earning power of the line, its physical value and its relationship to the other parts of the system, found that the continuation of the operation of this leased line as part of the system was desirable, upon proper terms, but that the terms of the present lease were too burdensome to permit their assumption by the reorganized company. It further found on the foregoing basis that a separation of the Terre Haute line from the system was not desirable if a new lease on the terms it found to be fair was to be accepted, but that rejection would be necessary if the offer of those terms was refused by the lessor's bondholders.

The principal objection of the Terre Haute interests has been to the provision of the plan that the lease may be adopted by the reorganized company only upon the condition, among others, that the obligation in respect to the payment of interest on the Terre Haute bonds is modified so that they will bear fixed interest of 2.75% per annum, and, in addition, interest at 1.5% contingent on system earnings on the same basis as new general mortgage bonds, Series A. This is the approximate equivalent of allotting fixed interest bonds for 70% of the Terre Haute claims and contingent interest, or income bonds for the remaining 30%.

In 1921, when the Terre Haute lease was executed, the annual fixed charges of the Milwaukee system were approximately $20,000,000, and the annual interest on the Terre Haute bonds approximately $900,000, or less than 5% of the system fixed charges. As shown above, the Commission found, even on the basis of that relationship, that "the terms upon which the property was acquired were improvident and to that extent adversely affected the financial condition of the St. Paul." (*Chicago, Milwaukee & St. Paul Investigation*, 131 I. C. C. 615, 657) The Commission has now found that conditions have so profoundly changed that the reorganized company can safely assume annual fixed charges in the amount of only $4,270,000, the payment of all other interest to be contingent upon earnings. Of that amount, $1,286,000 is required annually on the equipment necessary to operate the system. Another half million dollars must go to the Reconstruction Finance Corporation on account of the emergency loan made by that agency during the depth of the depression. This only leaves approximately $2,500,000 available annually as fixed interest for all other creditors having liens, both on the 10,000 mile Milwaukee system and the 300 mile Terre Haute property. What the Terre Haute is seeking, therefore, in the face of the tremendous cut which has become necessary in the amount of the system's total fixed charges, is that it continue to receive as a fixed charge, out of this $2,500,000, its full interest exceeding a million dollars. This is approximately 69% of what would remain for all bonds other than those allotted to the Reconstruction Finance Corporation. It is the demand of bondholders having a lien on a bare 3% of the system mileage who received less than 5% of the system fixed charges when the lease was made. In rejecting this contention the Commission said:

"Retaining the present fixed rental payments and

> at the same time keeping total fixed interest charges to about $4,270,000 a year, as provided in our plan, would thus necessitate reducing the amount of new first mortgage bonds issuable by $10,500,000. Such reduction would mean a substantial sacrifice by the creditors of the debtor who are to receive first-mortgage bonds in part settlement of their claims—a sacrifice in favor of the Terre Haute bondholders which, in our opinion, would be entirely inequitable." (R. 1303)

In the event that the offer to the Terre Haute fails to receive the approval of substantially all of the Terre Haute bondholders, the plan provides that the lease shall be rejected as of the date on which the District Court determines that the requisite approval has not been obtained. (R. 1331) In furtherance of their effort to force an outright adoption of the lease and thus secure the full amount of their annual interest out of the greatly reduced fixed charges of the reorganized company, the Terre Haute bondholders attack this provision of the plan as constituting an error of law.

Both in the District Court and in the Circuit Court of Appeals the contention was stressed by them that the rejection of a lease during the reorganization of a railroad, whether it be by the trustees in bankruptcy during the course of administration or by a provision of the plan of reorganization, must be given effect *as a matter of law* as of the date when the petition in bankruptcy had been filed. It was contended that this was an immutable rule of law which prevented the Commission from prescribing any other date in its approved plan of reorganization.

The Terre Haute interests urged as a corrollary of this proposition, that they became thereby entitled to a very large preferred claim against the trust estate, large enough, according to some of their counsel, to make the entire plan of reorganization lacking in feasibility. Their theory was that the "dating back" of the rejection of the

lease to the inception of the bankruptcy proceeding entitled them to the "profits" assumed to accrue from the operation of these lines during those years in excess of the rentals which had been paid to them by the trustees in bankruptcy in accordance with the terms of the lease itself.[1]

The District Court examined with great care both the facts and the law applicable thereto in passing upon this contention. It found that the Interstate Commerce Commission was bound by no such immutable and controlling rule of law, that the provision which the Commission had included in the plan was valid and authorized by statute, and that the challenged provision along with the other provisions of the plan which had been certified to it by the Commission should be approved.

As to the contention that the rejection of a lease by provision in a plan must date back to the time when a petition in bankruptcy was filed, the District Court said:

> "The objectors call attention to the rule prevailing in equity receiverships that a receiver is allowed a period within which to determine whether or not he shall affirm or disaffirm existing leases and that his action relates back to the date of the institution of the proceedings. Reliance is placed upon *American Brake Shoe & Foundry Company* v. *New York Railways*, 282 Fed. 523, and other similar cases and upon the case of *Palmer* v. *Palmer*, 104 Fed. (2nd) 161, which arose out of the New Haven reorganization. Examination of the authorities discloses that this rule is one designed for the protection of the receiver or the trustee. It is based on the theory that it is proper that he should have a reasonable time in which to elect to affirm or disaffirm and if he does elect to disaffirm, he should not be required to pay the rental fixed to the

[1] The assumption that such profits existed ignores the fact that the operation of the Terre Haute lines as part of the Milwaukee System was in effect a joint enterprise to which the system, in large measure, contributed the traffic. (R. 2213)

date of disaffirmance. As a rule, the leases which are disaffirmed are those which are unprofitable and the cases in which the principle is announced are cases in which the earnings were less than the rental provided. The authorities seem to recognize that in a given situation there may be special equities which will afford a basis for a different result. This suggestion is made in *Pennsylvania Steel Company* v. *New York City Railway Company*, 198 Fed. 721, and *Pennsylvania Steel Company* v. *New York City Railway Company*, 225 Fed. 734, and the principle is approved in the *Westinghouse Case* relied upon by the objectors.

"Sub-division (b) of Section 77 provides that the Plan of Reorganization may reject unexpired leases and further provides that the adoption of an unexpired lease by the Trustees of the Debtor shall not preclude a rejection of such lease in the Plan. Subdivision (c) (6) of Section 77 provides that after a lease is rejected and if the lessee, with the approval of the Judge, shall elect no longer to operate the leased line, it shall be the duty of the lessor, at the end of a period to be fixed by the judge, to begin the operation of such line unless the Judge, upon the petition of the lessor, shall decree, after hearing, that it would be impracticable and contrary to the public interest for the lessor to operate the said line, in which event it shall be the duty of the lessee to continue operation on or for the account of the lessor until the abandonment of such line is authorized. The first of these provisions clearly distinguishes between the right of the Trustees to disaffirm and the right to disaffirm in the Plan itself.

"In this case, no action has been taken by the Trustees to disaffirm the Terre Haute lease and the alternative of disaffirmance, if carried out, will be a disaffirmance by the Plan itself as distinguished from disaffirmance by the Trustees. The record in this proceeding shows that early in the reorganization the Trustees made application to the Court for authority to pay rental obligations arising under the Terre Haute lease and the Court made an order authorizing

the payment of interest due, or to become due, upon the Terre Haute bonds, which interest, as previously pointed out, the Debtor is required to pay by way of rental. That order, made in 1935, has not been modified and pursuant to it the Trustees have paid the interest on the Terre Haute obligations as it came due. Such interest, constituting rental, has been paid to the holders of the bonds and the bondholders have accepted it. They cannot demand more and they are the real parties in interest on the Terre Haute side. The parties, therefore, have carried on under the lease in the same manner as prior to the bankruptcy proceedings. It would be unreasonable to require the lessee, who has paid the stipulated rental to third parties pursuant to Court order, to account for a further sum for the same period covered by the rental so paid. It would seem in accordance with equitable principles to treat the transaction as closed up to the point to which rental is paid and accepted." (R. 1881-1883)[1]

The District Court held that, in Section 77, Congress had specifically authorized the Commission to provide in a plan of reorganization for the rejection of leases. It construed the statute as carrying with that right the authority to prescribe appropriate terms and conditions including the effective date of disaffirmance. This conclusion is supported by the plain provisions of the statute itself. Thus Section 77(b) provides in part:

"A plan of reorganization * * * may reject

[1] Numerous authorities declare the rule of law which is thus stated by the court. In addition to those cited in the portion of the opinion quoted above see *Sunflower Oil Co.* v. *Wilson*, 142 U. S. 313, 322 (1892); *City and County of Denver* v. *Stenger*, 295 Fed. 809, 817-8 (C. C. A. 8th, 1924); *In re United Cigar Stores of America*, 69 F. (2d) 513, 516-7 (C. C. A. 2nd, 1934) cert. den. sub. nom.; *Reisenweber* v. *Irving Trust Co.*, 293 U. S. 566; *Westinghouse Electric & Mfg. Co.* v. *Brooklyn Rapid Transit Co.*, 6 F. (2d) 547, 551 (C. C. A. 2nd, 1925); *Oscar Heineman Corp.* v. *Nat Levy & Co.*, 6 F. (2d) 970, 973 (C. C. A. 2nd, 1925); *Harris Trust & Savings Bank* v. *Chicago Rys. Co.*, 39 F. (2d) 958, 965 (D. C. Ill., 1929); Finletter, *The Law of Bankruptcy Reorganization* pp. 229-231 (1939); and Fletcher, *Cyclopedia of Corporations*, Vol. 16, Sec. 7794 (1933).

> contracts of the debtor which are executory, in whole or in part, *including unexpired leases; and may include any other appropriate provisions not inconsistent with this section.*"

Nothing in the section makes inappropriate a determination by the Commission in the plan of the date, under the circumstances considered, when such rejection should be effective. In addition, the clear intent to give the Commission power to deal with the particular problem before it so as to achieve a fair and equitable result is indicated by a further provision in the section of the Act in respect to "claims":

> "The adoption of an executory contract or unexpired lease by the trustee or trustees of a debtor shall not preclude a rejection of such contract or lease in a plan of reorganization approved hereunder, and any claim resulting from such rejection shall not have priority over other claims against the debtor because such contract or lease had been previously adopted."

The Commission's plan directed that the provisions respecting the Terre Haute lease should be submitted by the reorganization managers to the Terre Haute bondholders before the court could declare a rejection of the lease. It also provided, in the event of rejection, for compensation to the Terre Haute bondholders as unsecured creditors of the debtor for any claims in respect thereto which the court might allow. In its report accompanying the plan, the Commission said, under the heading "Unsecured Claims":

> "These 55,000 shares of new common stock are in principle distributable to all general claimants whose claims shall be allowed by the court. Besides the $445,162 of recorded unsecured claims, as of September 30, 1937, there are the potential claims which may arise from the possible rejection of the Terre Haute lease and the guaranty of the Terre Haute income bonds, * * *." (R. 2261)

In its supplemental report, the Commission said:

> "In the event the proposals be rejected, and the alternate provisions of the plan with respect to the Terre Haute become operative, all claims for damages growing out of the unfulfilled provisions of the rejected lease and the guaranty of the income bonds, in order to be recoverable at all against the debtor's estate, as we understand the matter, would have to be filed with the court in this proceeding. It is also our understanding that such claims would have the status of general unsecured claims. Accordingly, the holders of such claims, to the extent allowed by the court, would participate with other general unsecured creditors in the distribution of such new securities as are provided and available under the plan." (R. 1304)

The District Court gave full consideration to all of the contentions of the Terre Haute interests to support their proposition that the reorganized company must adopt the existing lease *in toto* or that the plan would be vitiated. (R. 1876-1885) In so doing it had before it not only the evidence presented in the proceedings before the Commission and the findings and conclusions of the Commission itself, but also extensive evidence presented to the District Court by the Terre Haute group. (R. 1684-1722) It discussed these objections in minute detail, expressed its opinion on each of them and finally concluded:

> "The Court feels that the Commission, in dealing with the Terre Haute interests, handled a difficult situation in a very creditable manner and evolved a Plan which is fair and equitable, all things considered." (R. 1885)

Without discussing the extensive findings appearing in the Commission's reports or the comprehensive treatment of the matter by the District Court, the Circuit Court of Appeals held as follows:

> "It is quite impossible to approve of the disposition of the Terre Haute bond issues without having more specific findings. Whether this lease should not

be now terminated presents a separate question, which can only be determined when findings are made." (R. 2314)

No indication was given of the nature of such required findings or of the asserted inadequacy of the record considered by either the Commission or the District Court or of the findings which they had made. We submit that the Circuit Court of Appeals was not justified in holding that further findings were necessary and instead that the findings were sufficient and the conclusions quite inescapable. The Commission acted within its jurisdiction, its determination was made in the light of controlling facts of record and there was no error of law.

7. CHICAGO, MILWAUKEE & GARY MORTGAGE.

The Commission found that the Gary was projected as an outer belt line around the Chicago district, but only disconnected portions were built. (R. 1308, 1309) These are joined by trackage rights over a competing line. (R. 1309) The Commission's findings as to the onerous terms of this trackage agreement appear at R. 1309.[1]

The original cost of the Gary property was $2,199,857, the cost of reproduction new $2,662,130, the cost of reproduction less depreciation $1,795,017, and the value of lands

[1] In its report on *Chicago, Milwaukee & St. Paul Investigation*, 131 I. C. C. 615 (1928), the Commission criticised the management of debtor's predecessor for acquiring the Gary in 1921, declaring that "undoubtedly the Gary was another drain upon the St. Paul which was incurred at a most inopportune time." (p. 662) It also said, "Acquisition of control by the St. Paul of the Terre Haute and also of the Gary was authorized by division 4 in *Acquisition of C., T. H. & S. E. Ry. by C. M. & St. P. Ry.*, 70 I. C. C. 20, and *Control of C. M. & G. Ry. by C. M. & St. P. Ry.*, 71 I. C. C. 124. In neither case should the acquisition have been approved upon the terms and conditions proposed. No opposition was offered and the records were, therefore, *ex parte*. Both cases illustrate the desirability of independent inquiry and investigation by the commission, so far as practicable, in uncontested matters of this character." (p. 663)

and rights, $488,991. (R. 1311; I. C. C. Bur. of Valuation Rept. on Elements of Value, Sheet 2)

In the six year period 1922-27, the Gary had an average yearly deficit of $58,908 before interest of $150,000 on its outstanding bonds. (R. 1309) In 1928 and 1929 it earned $133,350 and $180,622, respectively, for that interest. (R. 1309) After 1930, the Commission found that no separate records were kept, but that the estimates made on the basis described by the Commission showed that in 1933, 1934 and 1936 the property of the Gary earned for interest $142,000, $60,000 and $54,161, respectively. (R. 1309)

The Commission discussed the fact that a substantial part of the freight movement over the Gary is "bridge traffic" which could have been moved, at the debtor's option, over other lines of the debtor. (R. 1310) It found that in 1928, for example, this bridge traffic produced revenues of $325,537, of which $108,839 came from commercial traffic and $216,698 from company material, whereas in 1936 the commercial bridge traffic produced only $4,523 in revenues and the company material produced $222,912. (R. 1310) The Commission stated and considered the evidence showing that if the bridge traffic had been routed over the other line of the debtor, the Gary would have had a deficit in 1936 of $45,816, before interest, and similar deficits of $5,187, $34,000, and $84,000 in 1928, 1933 and 1934, respectively. (R. 1310) It further considered, however, the worth of the traffic contributed by the Gary to the debtor's system, and found that the 1936 revenues derived by the debtor from traffic originated, terminated, or interchanged with other lines at points on the Gary were $418,316, of which $307,285 was derived from traffic to or from Rockford, and $110,031 to or from all other stations on the Gary. (R. 1310) It described the basis of the estimates of what the Gary produced for

the system in 1936 ($48,933) and the similar estimates of $129,927 in 1928, $145,210 in 1929, $25,218 in 1933 and a deficit of $32,813 in 1934. (R. 1310-1311)

The Commission then found:

> "It is apparent to us that the Gary property, split into three disconnected portions as it is, and so dependent upon the Elgin, Joliet & Eastern, a competing line, for the much restricted trackage rights described, has very limited earning power as a railroad. The property and facilities at Rockford, however, are fairly productive of revenues not only for the Gary property as such but also for the debtor's system, as above indicated." (R. 1311)

Based on this finding, the Commission further found that the plan which it had originally approved should be modified in favor of the Gary as described at R. 1311.

The District Court likewise passed upon the claims of the Gary's bondholders. It said:

> "The Gary line has a record of poor earnings. Some evidence was introduced tending to show the scrap value of the property. The property cannot be scrapped except through abandonment pursuant to appropriate order by the Commission. Moreover, no one has seriously suggested that that procedure should be followed.
>
> "The Commission gave further consideration to the Gary claim upon petition for modification of the report and concluded that the Gary bonds should receive 75% in new preferred stock and 25% in new common stock, whereas under the original plan only common stock was to be allotted to the Gary bondholders. There is nothing in the record which would justify better treatment for this group." (R. 1890-1891)

The Circuit Court of Appeals merely stated, as to the Gary, that more findings were necessary. No reference was made to the fact that the Commission had carefully considered the Gary in both of its reports in this case,

and had made specific and comprehensive findings regarding every issue presented in connection with it. Likewise, no reference was made to the review by the District Court or to its opinion, findings and conclusion thereon.

(e) The Decision Below Is Not Required by the Opinion in the Consolidated Rock Products Case and Would Defeat the Purpose of Section 77.

The view of the Circuit Court of Appeals that its decision was required by the opinion in *Consolidated Rock Products Co.* v. *Du Bois*, 312 U. S. 510 (1941) is erroneous. Instead, the decision is, we believe, in direct conflict with the decision in that case. The reorganization plan under consideration there involved a comparatively small holding company and its two subsidiaries, all three of which had securities in the hands of the public. No real effort had been made to determine the earning power of the enterprise as a whole or of any of its parts. There was some highly questionable evidence of "physical value", and the proof showed that there had been no net operating profit since 1929. There was left undetermined a very large claim asserted by the subsidiaries against the parent. Nevertheless, the District Court allowed the stockholders of the parent company to participate in the distribution of new securities. The fatal infirmity of the plan was not the form of the opinion of the District Court approving it, but rather the absence of the vital evidence necessary to sustain it. Indeed, the evidence before the District Court was directly opposed to the action taken by it, and so far as appears there was not a single piece of evidence which supported the plan.

The *Rock Products* plan was rejected on two grounds. On the first, Mr. Justice Douglas said:

"In the first place, there must be a determination of

what assets are subject to the payment of the respective claims. This obvious requirement was not met." (312 U. S. at 520)

"In the second place, there is the question of the method of valuation. From this record it is apparent that little, if any, effort was made to value the whole enterprise by *a capitalization of prospective earnings.*" (312 U. S. at 525)

"* * * The criterion of earning capacity is the essential one if the enterprise is to be freed from the heavy hand of past errors, miscalculations or disaster, and if the allocation of securities among the various claimants is to be fair and equitable. *In re Wickwire Spencer Steel Co.*, 12 F. Supp. 528, 533; 2 Bonbright, Valuation of Property, pp. 870-881, 884-893. Since its application requires a prediction as to what will occur in the future, an estimate, as distinguished from mathematical certitude, is all that can be made. But that estimate must be based on an informed judgment which embraces all facts relevant to future earning capacity and hence to present worth, including, of course, the nature and condition of the properties, the past earnings record, and all circumstances which indicate whether or not that record is a reliable criterion of future performance. A sum of values based on physical factors and assigned to separate units of the property without regard to the earning capacity of the whole enterprise is plainly inadequate. See Finletter, The Law of Bankruptcy Reorganization, pp. 557, *et seq.* But hardly more than that was done here. The Circuit Court of Appeals correctly left the matter of a formal appraisal to the discretion of the District Court. *The extent and method of inquiry necessary for a valuation based on earning capacity are necessarily dependent on the facts of each case.*" (312 U. S. at 526-27)

The Circuit Court of Appeals failed to observe the principle just stated that the Commission's action was necessarily dependent on the facts of *this* case, and must be

reviewed on that basis. We have called attention to the completeness of the Commission's reports. Its two reports show unmistakably that the Commission gave dominant weight to the earning capacity of the system and of its several mortgage divisions, recognizing, as this Court later held, that "The criterion of earning capacity is the essential one." Based upon such evidence, the Commission made a "capitalization of prospective earnings" which represents, we submit, an "informed judgment." Greater particularity could not have been expected by the Congress. In the quotation above, this Court stated that "an estimate, as distinguished from mathematical certitude, is all that can be made." Such estimates were made by the Commission on an extensive record and both courts below held that these estimates are supported by the evidence.

In examining a tax assessment in *N., C. & St. L. Ry.* v. *Browning*, 310 U. S. 362, 370 (1940) this Court held that:

> "* * * railroads, unlike farms and city lots and stocks and bonds, are not objects of exchange. The very notion of a 'full cash value' for a railroad is in many respects artificial. See 1 Bonright, The Valuation of Property, pp. 511-632. Whatever may be the pretenses of exactitude in determining such a 'value,' to claim for it 'scientific' validity, is to employ the term in its loosest sense."

Similarly, this Court refused to search for any such "delusive certainty" in *U. S.* v. *Morgan*, 313 U. S. 409, 417 (1941), even though in that case the task of the administrative agency was less difficult than here.

The second ground for rejecting the *Rock Products* plan was that it clearly violated the rule of the *Boyd* case. The Court said:

> "* * * In the first place, no provision is made for the accrued interest on the bonds. This interest is entitled to the same priority as the principal. * * * In the second place, and apart from the cancellation of interest, the plan does not satisfy the fixed principle of the

Boyd case even on the assumption that the enterprise as a whole is solvent in the bankruptcy sense. The bondholders for the principal amount of their 6% bonds receive an equal face amount of new 5% income bonds and preferred stock, while the preferred stockholders receive new common stock." (312 U. S. at 527)

Neither of those errors occurred here. Accrued interest was accorded the same priority as principal. The old stockholders were entirely excluded. Junior creditors were allowed to participate only to the extent that there was property available, carefully determined by the Commission. The Commission made the necessary practical adjustments, and provided "a simple, conservative capital structure" (cf. 312 U. S. at 531). Indeed, it was primarily because of those features of the plan that the appeals below were taken.

The Commission found the elements of physical value for these divisions, stated and gave dominant weight to the results of the comprehensive earnings studies for the various divisions, considered the degree of interdependence of the divisions, and then stated its judgment as to the values of the mortgage divisions in terms of the allocations of new securities. By so doing, it complied with the direction of Congress that it "state fully the reasons for its conclusions." (Section 77 (d)) It both effectuated the purposes of Congress and made an intelligent examination of its decision much easier than would have been the case if it had purported to resolve the many elements which entered into its final judgments in a single sum, "value" for each of the several mortgage divisions. Certainly there is nothing in the *Consolidated Rock Products* decision to indicate that such a searching examination and evaluation of the different railroad divisions as was made by the Commission in this case is fatally inadequate or that the Commission's conclusions, which have been held to be supported by the evidence, must be further sup-

ported by the statement of figures purporting to represent the single sum "value" of each division.

It is made entirely clear by the Commission's diligent but protracted and largely ineffectual effort to determine and report the final values of the railroads under the Valuation Act of 1913 that such a requirement not only would defeat the purpose of the Congress to accomplish the prompt reorganization of bankrupt railroads, but would make the legislation impractical and substantially unworkable. The requirement of findings is a realistic and practical one, intended to effectuate the administrative process and not to frustrate it by demands which cannot be met. This Court has never held that an administrative determination must have the formal niceties of a pleading at common law. The Commission here found and stated the values of the several mortgage properties in terms of earning power and of rights to future income rather than absolute values in terms of dollars and cents, and this, we believe, effectuates the intent of the statute.

IV.

PROCEEDINGS SHOULD BE REMANDED WITH DIRECTIONS TO AFFIRM ORDER OF DISTRICT COURT APPROVING COMMISSION'S PLAN OF REORGANIZATION.

It is submitted that the record before this Court clearly shows that the Commission complied with all of the requirements of Section 77, procedural and substantive alike, in formulating the certified plan of reorganization as was held by the District Court, and that the Circuit Court of Appeals was in error in holding that other and different findings by the Commission were required to sustain the validity of the plan, or that a different type of court review was required than that which the District Court followed in approving the plan.

Congress has required the Commission to perform a tre-

mendously difficult task in formulating a plan of reorganization for this property under which it can continue its public function under modern conditions of competitive transportation. Speaking of the reorganization of another large railroad system under Section 77, this Court said:

> "In the reorganization of a great railroad system like that here concerned, these various steps call for a degree of consideration and an extent of detailed work almost beyond the power of appreciation."[1]

In this, as in other railroad reorganizations, the large sums involved and the complexity of the mortgage structures have encouraged all junior claimants and some senior creditors to litigate to the bitter end every question of law and fact which ingenuity could devise. The proceedings before the Commission consumed four years and eleven months—from June 29, 1935, when the petition in bankruptcy was filed, to June 4, 1940, when the Commission's supplemental report and order were issued. This time was employed in the necessary study of the complicated facts required to prepare a plan of reorganization, and in the consideration of the many conflicting claims of creditor and stockholder interests, all vigorously presented. Litigation over the certified plan has already consumed more than two additional years.

All of the objections to the plan which were urged upon the Circuit Court of Appeals had been presented both to the Commission and the District Court, and ruled upon independently by each. In each instance the claim was grounded upon an asserted right to a larger proportionate share of one or more of the several classes of securities of the reorganized company for the objector, with a resulting diminution in the allocations to other creditor interests. The complaints were directed either to the findings and conclusions that the equity of

[1] *Continental Bank* v. *Chicago, Rock Island & Pacific Railway*, 294 U. S. 648, 679 (1935).

the old common and preferred stock had no value, or to the findings which the Commission made and the conclusions which it reached in carrying out the direction of Congress that the certified plan of reorganization "shall include provisions modifying or altering the rights of creditors generally, or any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise." (Section 77(b))

Never before in the long history of railroad bankruptcies have reorganizations been the subject of investigations which have been so searching and of consideration which has been so complete in their purpose to protect both public and private rights as those which the Commission has conducted under Section 77. This has been accomplished, however, at a cost in time and effort much greater than was involved in the equity practice, the evils of which Congress was seeking to remedy. To now hold that the Commission's plan representing many years of earnest work must go back to the Commission for further refinement in matters of form, is, we believe, contrary to the statute and subversive of both public and private interests.

We submit that the record shows that the Commission performed its duty under the Act in strict accordance with its provisions, that the record amply supported its findings and conclusions, and that no error of law was committed by it. Thereafter the District Court, considering the plan both upon the record before it and before the Commission, determined that the plan was lawful and conformed fully to the requirements of Section 77. If the Circuit Court of Appeals was in error, as we believe it was, in ruling that other and different findings are required in a railroad reorganization than those which the Commission has stated in its reports herein, expedition and orderly procedure will be accomplished by remanding the case with instructions to affirm the judgment of the District Court approving the Commission's plan.

The entire record is before this Court.[1] The District Court approved the plan pursuant to the statutory mandate that "After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied * * *." (Section 77(e))

We ask that this Court reverse the decision of the Circuit Court of Appeals and direct affirmance of the approval by the District Court, thus completing the statutory process for approval of the plan. Then the plan may be submitted forthwith to a vote of creditors and the remaining procedural steps taken as required by Section 77, so that the purpose of Congress in providing for the reorganization of this railroad in conformity with a plan formulated in the public interest may be accomplished without further delay.

Respectfully submitted,

KENNETH F. BURGESS,
DOUGLAS E. SMITH,
GEORGE RAGLAND, JR.,
Attorneys for Group of Institutional Investors.

FRED N. OLIVER,
WILLARD P. SCOTT,
Attorneys for Mutual Savings Bank Group.

SIDLEY, MCPHERSON, AUSTIN & BURGESS,
OLIVER & DONNALLY,
Of Counsel.

---

[1] The holding of this Court in *Story Parchment Co.* v. *Paterson Co.*, 282 U. S. 555, 567 (1931) is applicable here: "The entire record, however, is before this court with power to review the action of the court of appeals and direct such disposition of the case as that court might have made of it upon the appeal from the district court."

APPENDIX.

The provisions of Section 77 (11 U. S. C. A. 205) most pertinent in this case are the following:

"(b) A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include provisions modifying or altering the rights of stockholders generally, or of any class of them, either through the issuance of new securities of any character, or otherwise; (3) may include, for the purpose of preserving such interests of creditors and stockholders as are not otherwise provided for, provisions for the issuance to any such creditor or stockholder of options or warrants to receive, or to subscribe for, securities of the reorganized company in such amounts and upon such terms and conditions as may be set forth in the plan; (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; (5) shall provide adequate means for the execution of the plan, which may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations, the retention of all or any part of the property by the debtor, the sale of all or any part of the property of the debtor either subject to or free from any lien at not less than a fair upset price, the distribution of all or any assets, or the proceeds derived from the sale thereof, among those hav-

ing an interest therein, the satisfaction or modification of any liens, indentures, or other similar interests, the curing or waiver of defaults, the extension of maturity dates of outstanding securities, the reduction in principal and/or rate of interest and alteration of other terms of such securities, the amendment of the charter of the debtor, and/or the issuance of securities of either the debtor or any such other corporation or corporations for cash, or in exchange for existing securities, or in satisfaction of claims or rights or for other appropriate purposes; and may deal with all or any part of the property of the debtor; may reject contracts of the debtor which are executory in whole or in part, including unexpired leases; and may include any other appropriate provisions not inconsistent with this section.

"(c) (11) The Commission may direct such of its agencies as it may designate to file in the proceedings before the Commission a report, and additional or supplemental reports at such time or times as the Commission shall designate, of such data with reference to the property, business, earnings, and corporate organization of the debtor and such other facts as the Commission, after hearing if it deems necessary, shall determine to be necessary or helpful information for the purposes of the preparation of reorganization plans, and for the purpose of aiding in determining the method or formula of allocating earnings permitted by subdivision (10) of this subsection c. Such report or reports shall be prima facie evidence of the facts therein stated in any proceeding under this section. The actual cost of preparing said report or reports shall be certified by the Commission and shall be borne by the debtor's estate.

"(d) * * * After the filing of such a plan, the Commission, unless such plan shall be considered by it to be prima facie impracticable, shall, after due notice to all stockholders and creditors given in such manner as it shall determine, hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall

render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subsections (b) and (e) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. In such report the Commission shall state fully the reasons for its conclusions.

"The Commission may thereafter, upon petition for good cause shown filed within sixty days of the date of its order, and upon further hearings if the Commission shall deem necessary, in a supplemental report and order modify any plan which it has approved, stating the reasons for such modification. The Commission, if it approves a plan, shall thereupon certify the plan to the court together with a transcript of the proceedings before it and a copy of the report and order approving the plan. No plan shall be approved or confirmed by the judge in any proceeding under this section unless the plan shall first have been approved by the Commission and certified to the court.

"(e) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, here all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor

of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of such hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; (3) the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge, except that allowances provided for in subsection (*c*), paragraph (12) of this section, may be paid in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is hereby given power to approve the same.

"If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection (d) of this section. If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) of this section, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, within such time as the Commission shall specify, together

with the report or reports of the Commission thereon or such a summarization thereof as the Commission may approve, and the opinion and order of the judge: *Provided*, That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the equity of such class of stockholders has no value, or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any, or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance: *Provided further*, That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially affected by the plan, or that at the time of the finding the interests of such class of creditors have no value, or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests. For the purpose of this section the acceptance or rejection by any creditor or stockholder shall be in writing, executed by him or by his duly authorized attorney, committee, or representative. If the United States of America, or any agency thereof, or any corporation (other than the Reconstruction Finance Corporation) the majority of the stock of which is owned by the United States of America, is a creditor or stockholder, the interests or claims thereof shall be deemed to be affected by the plan, and the President of the United States, or any officer or agency he may designate, is hereby authorized to act in respect of the interests or claims of the United States or of such agency or other corporation. The expense of such submission shall be certified by the Commission and shall be borne by the debtor's estate. The Com-

mission shall certify to the judge the results of such submission.

"Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is required under this subsection holding more than two thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: *Provided*, That, if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e): *Provided further*, That if, in any reorganization proceeding under this section, the United States is a creditor on claims for taxes or customs duties (whether or not the United States has any other interest in, or claim against, the debtor, as creditor or stockholder), no plan which does not provide for the payment thereof shall be confirmed by the judge except upon the acceptance, certified to the court, of a lesser amount by the President of the United States or the officer or agency designated by him pursuant to the provisions of the preceding paragraph hereof: *Provided further*, That if the President of the United States or such officer or agency shall fail to accept or reject such lesser amount for more than ninety days after receipt of written notice so to do from the court, accompanied by a certified copy of the plan, the consent of the United States

insofar as its claims for taxes or customs duties are concerned shall be conclusively presumed. If the judge shall confirm the plan, he shall enter an order and file an opinion with a statement of his conclusions and his reasons therefor. If the judge shall not confirm the plan, he shall file an opinion, with a statement of his conclusions and his reasons therefor, and enter an order in which he shall either dismiss the proceedings, or, in his discretion and on the motion of any party in interest, refer the case back to the Commission for further proceedings, including the consideration of modifications of the plan or the proposal of new plans. In the event of such a reference back to the Commission, the proceedings with respect to any modified or new plan shall be governed by the provisions of this section in like manner as in an original proceeding hereunder.

"If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."